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IN THE

Supreme Court of the United States

OCTOBER TERM, 1947.

No.

THE NEW YORK, NEW HAVEN AND HARTFORD RAILROAD COMPANY, as successor to Howard S. Palmer, James Lee Loomis and Henry B. Sawyer, Trustees of the property of The New York, New Haven and Hartford Railroad Company, Debtor,

Petitioner,

—against—

RECONSTRUCTION FINANCE CORPORATION,

Respondent.

Petition for Writ of Certiorari to the United States Circuit Court of Appeals for the Second Circuit.

To the Honorable the Chief Justice and Associate Justices of the Supreme Court of the United States:

The petitioner, The New York, New Haven and Hartford Railroad Company, as successor to the Trustees of the property of The New York, New Haven and Hartford Railroad Company, Debtor, respectfully prays that a writ of certiorari issue to review the judgment of the United States Circuit Court of Appeals for the Second Circuit entered in the above cause on December 4, 1947, affirming an order of the District Court of the United States for the District of Connecticut entered on December 13, 1946. A timely petition for rehearing or for modification of opinion was filed, which was denied by the Circuit Court of Appeals on December 20, 1947.

Summary Statement of Matters Involved.

The petitioner herein asks the enforcement of a promise in writing made by Mr. Jesse H. Jones on behalf of the Reconstruction Finance Corporation (RFC) to the Trustees in Bankruptcy of The New York, New Haven and Hartford Railroad Company, on December 21, 1938, a promise that "if, in the reorganization . . . the claims of this Corporation have been fully paid, this Corporation will accept 4 per cent from the date of the bankruptcy in full settlement of the interest, regardless of the rate named in the face of the note" (R., p. 229, Exhibit B).

Subsequently to this promise of Mr. Jones, the amount of RFC claims was reduced from approximately $11,744,000 (R., p. 228) to a balance of about $2,612,000 on July 11, 1946—computed on the basis of the rate named in the face of the notes (R., p. 225). This reduction was effected by direct cash payments made by the Trustees under Court Orders in response to their petitions and by the application by RFC of the income received on collateral securities held by RFC.

At this point, July 11, 1946, the Trustees filed in the District Court a petition that is directly involved in the present application for certiorari. They petitioned for permission to make the final payment of the claims of RFC necessary to the complete fulfilment of the condition specified by Mr. Jones in the promise quoted above. This petition was similar to seven earlier petitions that had been granted and that had resulted in cash payments of nearly $2,000,000, differing from them only as follows: this payment would be the final one, would be made out of cash assets held by the Trustees without the necessity of selling any securities, and would be followed by a cancellation of the notes and a surrender of the collateral held by RFC (R., p. 222).

At the informal hearing on this last petition, RFC, acting through its new Chairman, Mr. Charles B. Hen-

derson, resisted on the grounds that Mr. Jones' promise was unenforceable for lack of consideration and lack of an acknowledgment by the Trustees (R., p. 233).

The promise of Mr. Jones had never before been withdrawn or repudiated (Statement by Hincks, *J.*, R., p. 247).

But for this objection by RFC, the claims of RFC would have been fully paid in cash about 13 months prior to the conclusion of reorganization, completely fulfilling the condition required by Mr. Jones. The unpaid balance was then so small that, in spite of the denial of the petition, the application of collateral income by RFC itself completely fulfilled the specified condition about 5 months prior to the conclusion of reorganization. And by final Court Order No. 1007, in the reorganization, the Trustees were compelled to make an additional cash payment of $433,456.44, this being the total balance of RFC claims, reckoning interest at 5 per cent instead of 4 per cent as promised. This final cash payment, plus credits previously made by RFC from income on collateral, caused the payments actually made within the specified time limit to be more than $800,000 in excess of the performance required by Mr. Jones as the condition of his promise. The equity of all other creditors in the trust estate was thereby reduced in exactly the same amount.

Meantime, appeal had been taken in the present case; and the final order of the District Court expressly provided for repayment in case of reversal. (See p. 27, *infra.*)

The District Court, in denying the petition of the Trustees for an order authorizing final payment on the terms of Mr. Jones' promise, made no reference to the large payments previously made by the Trustees, being unable to see any consideration for Mr. Jones' promise or any sufficient action or forbearance in reliance on it. In its memorandum of opinion (R., p. 250) nothing is said as to the jurisdiction or system of law by which the rights of the parties are governed.

In the Circuit Court of Appeals, 2d Circuit, it was contended by RFC that the enforceability of Mr. Jones' promise is determined by the law of the State of New York, where the contract of loan was made and where it was to be and was in fact in every respect performed. Counsel for your petitioner assented to this and called attention to an applicable statute of New York (Brief for Appellee in the C. C. A., p. 28, and Reply Brief for Appellant in the C. C. A., p. 5). Nevertheless, the Circuit Court of Appeals affirmed the decision of the District Court, its opinion being printed in the record, page 277, and also in 164 Fed. 2d 466.

The Circuit Court of Appeals expressly refused to determine by what system of law the validity of Mr. Jones' promise should be determined, although counsel for both parties agreed in that Court that the applicable law is the law of New York. In particular, it refused to apply the statutory law of New York which provides that a promise such as that of Mr. Jones "shall not be invalid because of the absence of consideration," the Court saying: "We refuse to decide this question, for, although it is true that we may affirm a judgment upon grounds not urged in the lower court, we may not reverse one upon such a ground" (R., p. 280).

This statement and decision are in direct conflict with the decisions of the United States Supreme Court, especially with the reasoning and decision of this Court in *Hormel* v. *Helvering*, 312 U. S. 552 (1941) and its companion case *Helvering* v. *Richter*, 312 U. S. 561 (1941). The former case is cited by the Circuit Court of Appeals as if it supported the decision being rendered.

In neither one of the opinions below are the material facts stated with sufficient fullness to show the merits of your petitioner's case or the number and character of the errors of interpretation and of law involved in the decision made. It would greatly ease the burden upon this Court if your petitioner could restrict its statement and argument to the one fatal error indicated above; but, in

order to show that there has been a plain miscarriage of justice and that there are special reasons why the public interest requires its correction, a review of the record is necessary.

The facts of record show that the promise of the RFC, made by Mr. Jesse Jones, its Chairman, was an enforceable promise, both at law and in business honor, wholly apart from the statutory law of New York. Those facts show that, because of inadequate consideration given to them, the refusal of enforcement will effectuate a plain miscarriage of justice, deeply injurious to the public interest.

The New York statute, on which your petitioner in part rests its claim, is no mere statutory "technicality". It is a principle of contract law, made applicable in New York to all men alike, in exact accord with the law merchant of many centuries and of every American jurisdiction (N. I. L., § 122). It was enacted on the recommendation of the New York State Law Revision Commission (Appendix to Brief, p. 81) and is based upon actual practice and business morality. The petitioner's claim is just and reasonable, whether determined by the statutes of New York, the Common Law of New York, or the law of any other Anglo-American or Civil Law jurisdiction.

The erroneous action of the Courts below has been caused largely by the fact that the facts of record have been embedded in a complex reorganization proceeding covering a period of twelve years, and finally by the misapplication in the Circuit Court of Appeals of a well-known rule of appellate procedure. Reversal is necessary both to do justice in a specific case and to avoid continued misapplication of that rule and continued conflict in the federal courts.

The reasons on which reversal is sought, briefly stated below, will be followed in the Brief by an outline of the important and relevant facts of record in chronological

order, in as condensed a form as seems possible, with occasional interpretative comment in footnotes.

Jurisdiction.

1. The jurisdiction of this Court is invoked under § 240, subdivision (a), of the Judicial Code, as amended by the Acts of February 13, 1925, c. 229, § 1, 43 Stat. 938, of January 31, 1928, c. 14, § 1, 45 Stat. 54, and of June 7, 1934, c. 426, 48 Stat. 926 (28 USCA, § 347(a)).

2. The judgment of the Circuit Court of Appeals sought to be reviewed is dated December 4, 1947 (R., pp. 283, 284). The order of the Circuit Court of Appeals denying the petition for rehearing is dated December 20, 1947 (R., pp. 306, 307).

Questions Presented.

Is it error for the Circuit Court of Appeals to refuse to determine or to apply the law of the State of New York on the sole ground that the question was not raised in the court below?

If the rights of the parties are in fact governed by a statute of the State of New York, is it error for the Circuit Court of Appeals to refuse to take notice of or to apply that statute on the sole ground that it was not called to the attention of the court below?

Was the creditor's written promise, made by the Reconstruction Finance Corporation through its Chairman, Mr. Jesse H. Jones, to the Trustees of the Bankrupt, to accept interest at 4 per cent in full satisfaction if the creditor's claims should be paid in full at that rate in the course of reorganization, a binding and irrevocable promise, either at the time it was made or after the prescribed condition had been in large part performed and the Trustees had petitioned the Court for permission to pay the balance?

REASONS FOR GRANTING CERTIORARI, FOR REVERSAL OF THE JUDGMENT BELOW, AND FOR A DECREE ORDERING REPAYMENT OR REMANDING THE CASE TO THE DISTRICT COURT FOR FURTHER PROCEEDINGS ACCORDING TO LAW.

I.

The refusal of the Circuit Court of Appeals to determine the rights of the petitioner in accordance with the statutory law of New York is in conflict with the decision and the reasoning of the Supreme Court in the companion cases of *Hormel* v. *Helvering*, 312 U. S. 552, and *Helvering* v. *Richter*, 312 U. S. 561, argued and decided together on March 17, 1941, and in conflict with other decisions of the Supreme Court of the United States, of the Circuit Courts of Appeals (including the Second Circuit itself), and of the Courts of the several States and England. The lower Court has thus perpetuated the conflict between Circuits that it was the purpose of this Court to wipe out in the two cases cited above.

II.

The failure of the Courts below to determine the rights of the parties in accordance with the law of the State of New York is contrary to the rule laid down in *Erie R. Co.* v. *Tompkins*, 304 U. S. 64 (1938), and with the policy underlying that decision. Both Courts below decided this case as if governed by rules of general common law when in fact it was governed by the law of a specific State.

III.

The decision of the Courts below is in conflict with Section 122 of the Uniform Negotiable Instruments Law, a rule directly derived from the law merchant and now a part of the statutory law of every American jurisdiction.

IV.

The legal operation of the original contract of loan and of its subsequent modification and partial discharge is determined by the law of the State of New York.

V.

The decision of the Courts below is erroneous, even regarding it as based upon some system of general Common Law and Equity, or upon such a system of New York or any other State. Before any withdrawal or denial of the validity of Mr. Jesse Jones' promise, the final cash payment as required by him was on the verge of performance; and that final payment was in fact received by RFC within the time limit.

VI.

The promise, the enforcement of which has been refused, was made by Mr. Jesse Jones, a high officer of the United States, on behalf of the Reconstruction Finance Corporation, organized and maintained by the Government for the public welfare. It was made to Trustees in Bankruptcy appointed by the District Court to maintain public railway service, to distribute assets fairly among thousands of creditors, and to restore the Debtor company to solvency and operating efficiency. Refusal of enforcement directly and injuriously affects the public interest; it decreases the assets available to other creditors and gives them to a creditor with no legal or moral right thereto; and it effectuates a plain miscarriage of justice.

It is believed that the refusal of the successor of Mr. Jones to honor his promise, and the failure of the Courts below to enforce it, are due primarily to the fact that the

petition of the Trustees for Court Order No. 891, was one small incident in a twelve year reorganization proceeding in bankruptcy. The great flood of administrative orders, testimony, correspondence, and records of litigation through the Courts and before the Interstate Commerce Commission, fills many volumes.

At the informal hearing in the District Court, where RFC for the first time repudiated Mr. Jones' promise, it was impossible for Court or Counsel to remember or to present all the factors relevant to the issue, even though all those factors were embedded in the record of the reorganization proceeding of which that hearing formed a part. Those factors are contained in the Transcript presented to the Circuit Court of Appeals and now presented here. In order to understand that Transcript of Record and to interpret and properly evaluate the factors included therein, a condensed outline of events, in chronological order, is presented in the brief. It is hoped that this outline, with occasional explanatory comment, will serve as an Index-Digest of the Transcript, presenting to the Court a brief history to which detailed argument may be related.

WHEREFORE, it is respectfully submitted that this petition for a writ of certiorari should be granted.

HERMON J. WELLS,
Attorney for Petitioner.

ARTHUR L. CORBIN, SR.,
H. H. CORBIN,
Of Counsel.

IN THE

Supreme Court of the United States

OCTOBER TERM, 1947.

No.

THE NEW YORK, NEW HAVEN AND HARTFORD RAILROAD COMPANY, as successor to Howard S. Palmer, James Lee Loomis and Henry B. Sawyer, Trustees of the property of The New York, New Haven and Hartford Railroad Company, Debtor,

Petitioner,

—against—

RECONSTRUCTION FINANCE CORPORATION,

Respondent.

BRIEF IN SUPPORT OF PETITION.

Opinions Below.

The District Court's opinion, which is not officially reported, is in the record at pages 250-257. The opinion of the Circuit Court of Appeals (R., pp. 277-282) is reported at 164 F. 2d 466, sub nom. *Palmer et al.* v. *Reconstruction Finance Corporation.*

Jurisdiction.

(Stated at page 6 of petition, *supra.*)

Statement of the Case.

Outline of Negotiations and Proceedings Between RFC and the New Haven Trustees Relating to Interest on Loans.

1933

Prior to the New Haven's reorganization proceedings, of which this case is a part, the New Haven Railroad borrowed from the Reconstruction Finance Corporation $7,699,778.34 (R., pp. 17, 30), giving its promissory notes bearing interest at 5 per cent (R., p. 222), and as collateral therefor a large assortment of income-bearing securities (R., pp. 30, 31). This transaction occurred in New York City, and the notes were payable there (R., p. 58). Prior to the proceedings RFC accepted 4 per cent interest in place of 5 per cent as provided in the notes (R., p. 222).

At about the same time the New Haven also borrowed from the Federal Emergency Administrator of Public Works $4,800,000, this indebtedness being evidenced by its promissory notes, bearing interest at 4 per cent (R., p. 13) and secured by other items of collateral (R., p. 117). (These notes and collateral were acquired by RFC prior to November 10, 1938 (R., p. 228).)

1935

Oct. 23 Petition for reorganization filed and approved (R., pp. 4, 5).

Nov. 8 Trustees appointed by the Court (R., p. 5).

Dec. 13 Letter of Jesse Jones, Esq., Chairman of RFC, in reply to a letter of the Trustees, stating policy of RFC on railroad loans and promising reduction to 4 per cent "if your Railroad Company pays interest in full in cash to date and continues currently to pay interest on its indebtedness to this Corporation" (R., pp. 59, 67).

Dec. 16 Acknowledgment with thanks by Trustees, stating intention to file petition accordingly, and asking information as to income on pledged collateral (R., pp. 60, 68).

Dec. 18 Reply of RFC stating that such income might be received by the Railroad as formerly (R., pp. 60, 69).

1936

Jan. 15 Court Order No. 31, permitting Trustees to pay interest at not exceeding 4 per cent (R., p. 15).

Jan. 16 Payment by Trustees, at Federal Reserve Bank of New York, of $112,243.36 interest at 4 per cent (R., pp. 26, 48-51, 90-91, 96, 105). Thereafter, RFC instructed Bank not to receive any further interest from Trustees (R., p. 49).

Feb. 27 Check for $1,476.76, further interest at 4 per cent, sent by Trustees to Bank, never cashed (R., pp. 26, 50, 91).

Mar. 3 Letter of RFC in response to letter from Trustees dated February 18, stating that interest would thereafter be paid out of income on collateral and that this would be collected and received by RFC (R., p. 70).

Mar. 14 Inquiry from Trustees whether interest so retained would be at 4 per cent or 5 per cent and whether RFC would retain the excess income (R., p. 71).

Mar. 21 Reply by RFC that it "will accept 4 per cent in full settlement" and that income in excess of "past due and current interest at 4 per cent" would be applied on principal (R., p. 72).

Apr. 4 Letter from Counsel for Trustees saying that right of RFC to retain and apply income from collateral was not challenged (R., p. 73).

Sept. 28 Letter from RFC, setting forth terms proposed by the Trustees and tentatively assenting thereto, providing that the Trustees would obtain a new Court Order in lieu of unsatisfactory Order No. 31 and would "take all appropriate steps to render available to RFC" all sums realized from all the collateral pledged to RFC, RFC promising to "reapply" such sums from October, 23, 1935, to interest at 4 per cent instead of 5 per cent, remainder to be applied to principal, and to make final settlement at 4 per cent if at final reorganization all interest had been kept paid at that rate. If not so paid, "Nothing in this arrangement contained shall be construed as a waiver by RFC" of its right to interest at 5 per cent (R., pp. 26-28).*

Oct. 5 Petition by Trustees for new instructions, setting out RFC letter of September 28 and noting that other creditors asserted that the arrangement would constitute a "preference" of RFC (R., pp. 17-34).

Nov. 2 Court hearing for purpose of defining issues to be dealt with by Order No. 102 (R., pp. 35-42).

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* The terms here proposed are consistent with the earlier letter of Mr. Jones, March 21, 1936, which was in plain promissory terms. The present letter, however, proposes additional action by the Trustees, *i. e.*, to procure a new order.

—— Answer and Statement of Claim by RFC (dealing largely with right of RFC to collect and apply income from collateral), repeating the terms stated in letter of September 28 as to reduction of interest to 4 per cent (R., pp. 42-56, especially pp. 51-52).

—— Affidavit of General Counsel Alley for RFC, stating place of making the loans, delivery of the notes and collateral, and place of payment (R., p. 58), and quoting the letters listed above as of December 13, 16, 18; March 3, 14, 21; and April 4 (R., pp. 57-73).

1937

June 16 Court's Memorandum of Decision on Petition for Order No. 102 (R., p. 89).

1938

Mar. 11 Final Order No. 102, on petition as amended (R., p. 104). In this Order the Court held:

1. That RFC "is entitled to receive and/or retain all income from and proceeds of collateral held by it . . ." (R., p. 104).

2. That RFC "is authorized and directed to apply such income and proceeds" to payment of interest "but at a rate not in excess of five per centum per annum, or to or toward the payment of principal . . ." (R., pp. 104-5).

3. That two payments made by the Trustees, of interest at 4 per cent, and received by RFC, under and in accordance with Court Order No. 31, operated in full discharge of all interest then due (R., p. 105).

4. That the assignment "of the so-called

'Grand Central Terminal advances' is wholly valid and effective" (R., p. 105).*

5-8, not here involved.

Nov. 10 Letter from Trustees, calling attention to the fact that RFC had been applying income from collateral on interest at 5 per cent, that such income had been and would be sufficient to keep interest currently up to date and reduce principal, and earnestly requesting "that the rate on these notes be reduced to 4 per cent as of November 1, 1938, and continued at that rate" (R., p. 228).

Dec. 21 Reply of Mr. Jones, from Washington, D. C., in full as follows:

"RECONSTRUCTION FINANCE CORPORATION
WASHINGTON

Jesse H. Jones
Chairman of the Board

December 21, 1938.

Dear Sirs:

Referring to your letter of November 10, beg to advise that if, in the reorganization of The New York, New Haven and Hartford Railroad Company, the claims of this Corporation have been fully paid, this Corporation will accept 4 per cent from the date of the bankruptcy in full settlement of the interest, regardless of the rate named in the face of the note.

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* The issue dealt with in par. 4, above, had been litigated by other creditors against RFC. The Court's Interlocutory Memorandum of Decision on this issue, made February 25, 1938, is reported in *In re New York, N. H. & H. R. Co.*, 25 F. Supp. 874 (D. C., D. Conn.). Par. 4, above, is the order resulting from that litigation.

Should the road not be able to arrange private financing on reasonable terms, we will be glad to discuss with it a loan to the reorganized company for this purpose and to effect a reorganization.

Yours very truly,

JESSE H. JONES,
Chairman.

Messrs. H. S. Palmer, J. L. Loomis
and H. B. Sawyer, Trustees
The New York, New Haven and
Hartford Railroad Company,
New Haven, Connecticut."

(R., p. 229.)*

1939

May 29 Trustees petition for Court Order No. 364 permitting sale of pledged collateral, with consent of RFC, for $208,000, and directing application on debt (R., p. 194).

June 9 Court Order No. 364 entered as asked (R., p. 197).

Aug. 1 Brief of RFC as intervenor before Interstate Commerce Commission, asserting that RFC had been adequately secured and (as a result of litigation in which the Trustees and RFC had participated) was on this date so secured "beyond question"; that between October 23, 1935 and

* This letter does not grant the request to reduce current applications to the 4 per cent rate, as had been unconditionally promised on March 21, 1936, and again at least "tentatively" promised on September 28, 1936. It is once more an express promise, however, that "this Corporation will accept 4 per cent from the date of the bankruptcy in full settlement, regardless of the rate named in the face of the note." This promise is conditioned as follows: "if, in the reorganization . . . the claims of this Corporation have been fully paid."

May 31, 1939, RFC had received $3,147,186.93 in reduction of its claim; that "it is convincingly clear that even if there is no reorganization effected herein, Reconstruction's claim will, in the course of time, be fully liquidated merely from the income and proceeds of its collateral;" that income from collateral for 1939 would be more than twice the current annual interest on the loans without any allowance for payments on principal from sales of collateral; that the collateral was such as was "not subject to treatment in the reorganization", so that "objections ordinarily made to the sale of system collateral do not exist"; and that the liquidation of the claim "can be substantially accelerated by the orderly sale of non system collateral".

In conclusion, RFC stated: "Reconstruction, along with other creditors, desires that a reorganization of the Debtor be effectuated. To this end, it is willing to make a concession in the interest rate charged on the R. F. C. loans provided it receives the treatment to which the collateral for its claim entitles it. On November 10, 1938, the Trustees of the Debtor addressed a letter (Ex. 203) to Mr. Jones, then Chairman of Reconstruction, requesting that the interest rate on Debtor's notes to Reconstruction be reduced to 4% per annum. In reply Mr. Jones stated (Ex. 204):" (Here the letter of December 21, 1938, above, was printed in full.)

The Brief then proceeded: "Recalculation of the interest on the R. F. C. loans at the rate of 4% instead of at 5%, the rate specified in the notes, would result in a saving to Debtor on the R. F. C. loans alone of approximately $320,000, as computed to December 31, 1939 (Tr. 2889). As indicated in Mr. Jones' letter, Reconstruction is willing to make this concession *provided*

it is made whole on its claim (both the R. F. C. and P. W. A. loans)" (R., pp. 112-135, especially pp. 133-134). (Italics theirs.)

Aug. 22 Trustees petition for Court Order No. 387 permitting a like sale of other pledged collateral for $72,000, and directing application on debt (R., p. 199).

Sept. 5 Court Order No. 387 entered as asked (R., p. 201).

1940

Sept. 9 Order No. 387 amended, with consent of RFC, by Court Order No. 387A (R., p. 202).

1941

Dec. 23 Trustees petition for Court Order No. 629 permitting sale of certain land pledged to RFC and held by it after foreclosure for price of $325,896 (R., p. 204).

1942

Jan. 9 Court Order No. 629 entered authorizing such sale and directing application on debt (R., p. 207).

1943

Apr. 19 Joint petition of Trustees and RFC for Court Order No. 693 for approval of stipulation for payment to RFC of $70,165.50 (R., p. 209).

May 7 Court Order No. 693 issued (R., p. 212).

1944

July 6 Trustees petition for permission by Court Order No. 758 to pay to RFC proceeds of other collateral, amounting to $217,656.65, with directions to RFC to make proper application (R., p. 213).

July 26 Court Order issued (R., p. 215).

Nov. 7 Court Order No. 779 issued, on oral motion of Trustees, for payment to RFC of the Trustees' share (about $231,915) of the proceeds from the sale of other collateral (R., p. 216).

(On pages 107-193 of the record, there are printed a number of statements, petitions, and Court Orders showing the improving condition of the Debtor's estate and of its cash assets between 1938 and 1945 and the decreasing interest rates at which the Trustees were able to finance. Acting by Court Order, the acquisition of railroad equipment was financed at interest rates decreasing from 4% to 1.63%, a reduction in the rate of interest from 4% to 2½% on certain equipment trust certificates held by RFC was effected (see, also, *N. Y., N. H. & H. R. Co. Equipment Trust Certificates* (1940), 240 I. C. C. 622), and the secured claims of seven banks in the aggregate amount of $12,472,604 were discharged by cash payments aggregating $10,692,642.)*

1945

Jan. 29 Letter from Trustees, stating that payments had reduced the principal sums of the RFC 5 per cent notes from $7,699,778.34 to $4,083,111.37 and the principal sums of the PWA 4 per cent notes (held by RFC) from $4,800,000 to $1,333,588.39. This letter then proceeded thus:

> "Having in mind current interest rates and the rates at which the government is able to borrow money, and also the substantial reductions in principal of R. F. C. and P. W. A.

* See, also, *New York Connecting R. R. Co. Bonds* (1940), 242 I. C. C. 275, (1945) 261 I. C. C. 845, where the Trustees and The Pennsylvania Railroad Company twice effected a reduction in interest rates on the bonds of their subsidiary, first from 4½% and 5% to 3½%, and later from 3½% to 2⅞%.

loans, as well as the fact that the loans are now so greatly oversecured, it is respectfully submitted that the interest rates of 5% and 4% per annum heretofore charged and applied by R. F. C. on the loans are excessive. Indeed the situation has changed radically for the better since December 21, 1938, when Mr. Jones wrote us that R. F. C. would accept a 4% rate from the date of bankruptcy if its claims were paid in the New Haven's reorganization.

"Accordingly, we now earnestly request a retroactive reduction in interest to 4% since October 23, 1935, on R. F. C. loans and a reduction to 3% on both R. F. C. and P. W. A. loans from now on" (R., pp. 230-232).*

Feb. 14 Charles B. Henderson, Esq., the new Chairman of RFC, replied as follows:

"Receipt is acknowledged of your letter of January 29, 1945, requesting a retroactive reduction in the interest rate to 4% since October 23, 1935, on loans made by this Corporation to The New York, New Haven and Hartford Railroad Company and a reduction in the interest rate to 3% 'from now on' on said loans, as well as on the notes evidencing the Public Works Administration's loans to the Railroad Company.

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* At this time completion of the express condition of Mr. Jones' promise of December 21, 1938, would have required payment of nearly $5,000,000 out of the Debtor's estate. *Had RFC acceded to this request of the Trustees, completion of the condition of full payment of its claims prior to the conclusion of the New Haven's reorganization would have been waived,* and the trust estate would have received the further benefit of the prospective reduction in interest to 3 per cent on the unpaid balance. *In this, there is no intimation that the Trustees had abandoned Mr. Jones' promise or that they had not many times acted in reliance on it. It would have been a breach of their duty as Trustees to abandon it.*

"This Corporation is unwilling to grant this request.

"However, this Corporation hereby consents to the reduction to 4% per annum, effective as of January 1, 1945, in the interest rate on the notes evidencing its loans to the Railroad Company, it being understood that the notes evidencing the Public Works Administration's loans to the Railroad Company shall continue to bear interest, according to their terms, at 4% per annum" (R., pp. 232, 233).*

July 10 Letter from Trustees requesting a reduction to 4 per cent in the interest rate on RFC loans from October 23, 1935, and stating that if RFC would grant said request, the Trustees were willing to petition the District Court for an order providing for the pledge with RFC of collateral formerly pledged with Railroad Credit Corporation, but held by the Trustees since the payment of Railroad Credit Corporation loans (R., p. 224).

Oct. 30 Trustees petition for Court Order No. 836, permitting sale of land for $667,930 and payment to RFC, with direction to apply (R., p. 217).

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* Not one word in this letter indicates that Mr. Henderson repudiated Mr. Jones' promise that final settlement should be made on the basis of 4 per cent from the beginning, provided RFC's claims were paid in full in the reorganization. The immediate reapplication at the 4 per cent rate of funds previously received by RFC and applied at 5 per cent is refused, as well as the prospective application at 3 per cent on the unpaid balance of the claims.

This letter left the right of the Trustees to a retroactive reduction of interest at 4 per cent from date of bankruptcy to January 1, 1945, conditional just as before, on full payment of the claims of RFC in the course of the reorganization.

Nov. 9 Court Order No. 836 entered (R., p. 220).*

1946

Feb. 21 Letter from Mr. Henderson denying Trustees' request of July 10, 1945 (R., p. 224).**

June 18 Letter from Trustees, stating that the principal sums of the RFC 5 per cent notes had been reduced to $2,190,912.96 and that the principal sums of the PWA 4 per cent notes had been reduced to $420,763.14—a reduction from the beginning of the proceedings from $12,486,054.53 to $2,611,676.10. The letter then continued:

> "In view of the continuance of low money rates, the fact that the loans have always been amply secured, and that most of the principal has been repaid even after application of the higher interest rate, we renew our request for a rate of 4% for the whole period of the proceedings with the understanding if you are agreeable that we will petition the Court for

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* By this petition and payment, following the line of previous ones, the Trustees were still acting in fulfilment of the condition stated in the letter of Mr. Jones on December 21, 1938. The new promise of Mr. Henderson on February 14, 1945 was wholly unconditional.

The action of the Trustees, in procuring the succession of Court Orders Nos. 364, 387, 629, 693, 758, 779 and 836, *was in every instance action that the Trustees were under no duty, legal or moral, to RFC to take* by virtue of the notes held by RFC. The sales of collateral and the payment to RFC of the proceeds could have been made by them only by Court Order, on a finding that the trust estate would thereby be benefited. The sum total of payments thus made out of proceeds so obtained amounted at this point to about $1,800,000.

** Had this second request to Mr. Henderson been granted, the effect would have been identical with that stated above in the footnotes to the first request made to him by the Trustees, except that, by the addition of the RCC collateral, the eventual full payment of the claims of RFC would have been rendered that much more certain.

an order providing for the pledge of the former Railroad Credit Corporation collateral with your Corporation in consideration of the reduction" (R., pp. 224, 225).*

June 25 Letter from Mr. Henderson denying this request (R., p. 225).

July 11 Petition of the Trustees for Court Order No. 891, alleging their unsuccessful attempts to procure the reapplication by RFC from the beginning of the proceedings of funds at the 4 per cent rate without full payment of its claims, and requesting authorization to pay and discharge the unpaid balance of the claims, out of current funds of the Debtor's estate, on the terms of Mr. Jones' letter of December 21, 1938, in order to fulfil the condition of his promise to "accept 4 per cent from the date of the bankruptcy in full settlement of the interest, regardless of the rate named in the face of the note." The balance of the principal debt to be paid in order to fulfil that condition was then about $1,741,000. The petition asked that upon this payment RFC be directed to surrender all notes and collateral (R., p. 222).**

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* At this time completion of the condition of Mr. Jones' promise would have required payment of about $1,741,000 out of the Debtor's estate. The Trustees were still willing to hypothecate additional collateral in consideration of the immediate reapplication by RFC at the 4 per cent rate of funds previously received and applied at 5 per cent, *which would have waived the completion of the condition.* Again there is no intimation that the Trustees had abandoned Mr. Jones' promise or that RFC had repudiated it.

** This petition, like similar petitions for hundreds of previous Court Orders, was in the course of the long reorganization proceedings, in which RFC had continuously asserted its claim as a creditor. *Here, the Trustees, having failed three times to induce Mr. Henderson to waive the condition prescribed by Mr. Jones, take the final step to complete its fulfilment by getting a Court Order for payment of the balance out of estate assets.*

Aug. 2 Hearing on this petition. In its answer, filed on this date at the hearing (R., p. 237), RFC asserted:

> "1. The letter dated December 21, 1938 . . . was not accepted or even acknowledged by said Trustees and does not constitute an agreement binding on RFC.
>
> "2. There is no agreement in existence requiring RFC to accept retroactively beyond January 1, 1945 interest at the rate of 4% per annum. . . .
>
> "5. RFC is unwilling to accept in settlement of its loans to the Principal Debtor payment on the basis proposed by said petition" (R., pp. 234, 235).*

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* Never before this date had RFC repudiated or attempted to withdraw the promise made by Mr. Jones. The promise was not an "offer" that required a "notice of acceptance". It was a promise in response to a request made by the Trustees in accordance with their duty as trustees of the estate. No return promise was requested; and no return promise could lawfully have been made by the Trustees without a special Court Order.

In this promise Mr. Jones invited the Trustees, by plain implication, to act in reliance on it, as men commonly rely on the given word of an officer and a creditor. Mr. Jones made his promise expressly conditional on full payment of the notes "in the reorganization". Actions in fulfilment of that condition followed in succession, down to the last full (and excessive) payment required by the District Court, each time with the knowledge and consent of RFC.

Until August 2, 1946, no grievance was expressed by RFC that the letter of December 21, 1938, "was not accepted or even acknowledged" by the Trustees. The record does, indeed, show that they had acknowledged, with thanks, Mr. Jones' earlier promise of December 13, 1935, a somewhat better promise than that of December 21, 1938.

The record does not show an acknowledgment of the latter promise for the reason that, if made, it would be wholly immaterial.

Mr. Jones received the benefits of at least six petitions and payments by the Trustees in partial fulfilment of the express condition of his promise; and Mr. Henderson received the benefit of

[Footnote continued on following page.]

Sept. 19 PWA 4 per cent notes paid in full.

Dec. 13 Memorandum of Decision and Order of the District Court Dismissing Petition for Order No. 891 (R., pp. 250-257).

1947

Jan. 11 Notice of appeal to Circuit Court of Appeals for the Second Circuit (R., p. 258).

Apr. 30 RFC 5 per cent notes paid in full on the basis of Mr. Jones' promise of December 21, 1938.*

May to Sept. Application by RFC of income from collateral aggregating $370,537.06 in excess of full payment on the basis of Mr. Jones' promise.

Aug. 20 Appellants' brief in Circuit Court of Appeals.

[Footnote continued from preceding page.]

the petition and payment under Court Order No. 836, after his own promise of February 14, 1945.

The repudiation of Mr. Jones' promise, as sustained by the lower Courts, reduced the value of the equity of all other creditors in the collateral held by RFC by the exact amount of the promised reduction.

The testimony at the hearing, though not extensive, should in itself be sufficient to establish the validity of Mr. Jones' promise. The Judge himself remarked that "The Trustees apparently were in a position on the basis of the collateral on this loan to obtain a lower financing had it not been for the promise contained in the letter" (R., p. 247, at bottom).

In determining the validity of that promise, the Court was not restricted, and did not regard itself as restricted, to the oral testimony offered at the hearing. That had to be determined, and the propriety of Order No. 891 now under review still has to be determined, by the entire record before the Court.

* Recalculation made on same basis as that used by RFC in its brief of August 1, 1939 to the Interstate Commerce Commission (R., p. 133—bottom of page).

Sept. 11 Consummation Order and Final Decree (Order No. 1007) of District Court in the reorganization proceeding. This order provided in part:

"*Continuation of Existing Corporation.* As authorized by the Plan, the [Reorganization] Committee has determined to use the Debtor * * * as the corporation which will carry out the Plan and to file a Certificate of Amendments of the Charter and Acts of Incorporation of the Debtor * * *. (Said corporation upon the filing of the Certificate of Amendments is hereinafter referred to as 'the Reorganized Company'.) The foregoing determinations of the said Committee are approved and the Reorganized Company shall be the corporate instrumentality for the consummation of the Plan" (Section 4 of Subdivision I).

"*Payment of Reconstruction Finance Corporation and Reallocation of Securities.* The Bankruptcy Trustees or the Reorganized Company is hereby authorized and directed to pay to Reconstruction Finance Corporation, in cash, at or immediately after the consummation date hereinafter fixed [*i. e.* September 18, 1947], the unpaid principal amount of said Corporation's claim against the Debtor, together with any interest accrued and unpaid to the date of such payment upon the basis stated in paragraph 7 of said Corporation's answer to the petition of the Bankruptcy Trustees dated July 11, 1946, for Order No. 891 with respect to said claim, provided, however, that said Corporation shall thereupon surrender and pay over to the Bankruptcy Trustees or the Reorganized Company, as the case may be, free and clear of any and all claim of said Corporation, any and all securities or other collateral held by said Corporation as security for the payment of said claim and provided further that if the final determination of the Bankruptcy Trustees' appeal from the Memorandum of Decision and

Order on Petition for Order No. 891 of this Court is contrary to said Memorandum of Decision and Order, said Corporation shall refund to the Bankruptcy Trustees or the Reorganized Company in cash, such amount as may be required as the result of such contrary final determination. The Collateral Trust Notes issuable under the Plan with respect to said claim shall not be issued and the new First and Refunding Mortgage Bonds and General Mortgage Income Bonds which under the Plan would have been pledged as collateral for such Notes, shall be reallocated, as provided in the Plan, among all secured creditors other than those whose claims are being satisfied wholly in New First and Refunding Mortgage Bonds or are undisturbed. * * *" (Section 6 of Subdivision I).

"*Transfer and Discharge.* Upon the consummation date:

> (i) all the business and affairs and the entire property and estate of the Debtor and the Secondary Debtors of every name and nature and all right, title and interest of Howard S. Palmer, James Lee Loomis and Henry B. Sawyer, as Trustees of the property of Debtor and the Secondary Debtors (herein called the 'Bankruptcy Trustees') * * * shall vest in and become the absolute property of the Reorganized Company * * *" (Section 3 of Subdivision II).

"*Pending Litigation.* The Reorganized Company shall be entitled to be substituted at its own cost and expense as a party in lieu of the Bankruptcy Trustees in any and all litigation to which the Bankruptcy Trustees may be a party on the consummation date, and to continue such litigation in the name of the Bankruptcy Trustees or in the name of the Reorganized Company" (Section 4 of Subdivision VIII).

Sept. 15 RFC's brief in Circuit Court of Appeals. In this brief it was stated at page 28:

"The Debtor's notes which were delivered to the RFC in evidence of RFC's loans to the Debtor were all executed and delivered in the City of New York, State of New York, and they are all payable at the Federal Reserve Bank of New York in the City of New York. Reference is made to Exhibit B [Appendix B to brief] which consists of a reproduction of relevant portions of the last remaining unpaid note of the Debtor evidencing a loan from the RFC. This note is typical with respect to the place of execution and delivery and the place of payment.

"From the foregoing facts it would seem clear that New York law should govern any question with respect to the payment of the RFC notes."

Sept. 19 Payment of $433,456.44 to RFC under provision of Court Order No. 1007 quoted above, also in excess of full payment on the basis of Mr. Jones' promise.

Nov. 10 Reply brief for appellants in Circuit Court of Appeals, referring to amendment made in 1936 to § 33(2) of the New York Personal Property Law.

Dec. 4 Opinion and Judgment of Circuit Court of Appeals (R., pp. 277-284).

Dec. 19 Petition of appellants to C. C. A. for Rehearing or for Modification of Opinion (R., pp. 285-304).

Dec. 20 Order of C. C. A. denying petition (R., p. 306).

Specification of Errors.

Both Courts below erred in refusing to enforce the promise of the Reconstruction Finance Corporation to accept interest at 4 per cent in full settlement; and the Circuit Court of Appeals erred in refusing to determine what system of law governs the case and in refusing to apply the statutory law of New York.

Argument.

Summary of the Argument.

(Point I) The refusal of the Circuit Court of Appeals to determine the rights of the petitioner in accordance with the statutory law of New York is in conflict with the decision and the reasoning of the Supreme Court in the companion cases of *Hormel* v. *Helvering*, 312 U. S. 552, and *Helvering* v. *Richter*, 312 U. S. 561, argued and decided together on March 17, 1941, and in conflict with other decisions of the Supreme Court of the United States, of the Circuit Courts of Appeals (including the Second Circuit itself), and of the Courts of the several States and England. The lower Court has thus perpetuated the conflict between Circuits that it was the purpose of this Court to wipe out in the two cases cited above.

(Point II) The failure of the Courts below to determine the rights of the parties in accordance with the law of the State of New York is contrary to the rule laid down in *Erie R. Co.* v. *Tompkins*, 304 U. S. 64 (1938), and with the policy underlying that decision. Both Courts below decided this case as if governed by rules of general common law when in fact it was governed by the law of a specific State.

(Point III) The decision of the Courts below is in conflict with Section 122 of the Uniform Negotiable Instru-

ments Law, a rule directly derived from the law merchant and now a part of the statutory law of every American jurisdiction.

(Point IV) The legal operation of the original contract of loan and of its subsequent modification and partial discharge is determined by the law of the State of New York.

(Point V) The decision of the Courts below is erroneous, even regarding it as based upon some system of general common law and equity, or upon such a system of New York or any other State. Before any withdrawal or denial of the validity of Mr. Jesse Jones' promise, the final cash payment required by him was on the verge of performance; and that final payment was in fact received by RFC within the time limit.

(Point VI) The promise, the enforcement of which has been refused, was made by Mr. Jesse Jones, a high officer of the United States, on behalf of the Reconstruction Finance Corporation, organized and maintained by the Government for the public welfare. It was made to Trustees in Bankruptcy appointed by the District Court to maintain public railway service, to distribute assets fairly among thousands of creditors, and to restore the Debtor company to solvency and operating efficiency. Refusal of enforcement directly and injuriously affects the public interest; it decreases the assets available to other creditors and gives them to a creditor with no legal or moral right thereto; and it effectuates a plain miscarriage of justice.

POINT I.

The refusal of the Circuit Court of Appeals to determine the rights of the petitioner in accordance with the statutory law of New York is in conflict with the decision and the reasoning of the Supreme Court in the companion cases of *Hormel* v. *Helvering*, 312 U. S. 552, and *Helvering* v. *Richter*, 312 U. S. 561, argued and decided together on March 17, 1941, and in conflict with other decisions of the Supreme Court of the United States, of the Circuit Courts of Appeals (including the Second Circuit itself), and of the Courts of the several States and England. The lower Court has thus perpetuated the conflict between Circuits that it was the purpose of this Court to wipe out in the two cases cited above.

The legal operation of a contract transaction between lender and borrower cannot be determined independently of some specific system of commercial law, enacted and enforced by some specific law-making jurisdiction. Since there is no "federal general common law" applicable to a commercial transaction such as the one here involved, the United States District Court could not make a proper determination of its legal effect without first selecting the particular State whose law is applicable and then determining what that law is. Without making these determinations (the question not having been raised by counsel for either party), the District Court refused enforcement of the promise made by the RFC (R., p. 257),* and later ordered payment in full on the 5 per cent basis, with an express provision for repayment if on appeal the order should be held to be erroneous. (See Court Order No. 1007, quoted *ante* at p. 27.)

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* Counsel for RFC agreed that if the District Court should find an obligation binding RFC, it could enter an order enforcing it (R., p. 249).

Believing that this decision was erroneous on "common law" grounds, and that the promise was enforceable, either because of action and forbearance in reasonable reliance upon it or because there was a sufficient consideration, the Trustees appealed to the Circuit Court of Appeals, in their brief still raising no question of the jurisdiction whose law is applicable. In the brief of the appellee RFC, however, it was asserted that the law of New York is the properly applicable law (see *ante*, p. 29). Counsel for the Trustees accepted this as correct, believing that the common law of New York is no different from that of the other States; and for the first time they became aware of the existence of the New York statute referred to in the introductory statement of the facts herein, quoted in the opinion of the Circuit Court of Appeals. This statute reads as follows:

> "An agreement hereafter made to change or modify, or to discharge in whole or in part, any contract, obligation, or lease, or any mortgage or other security interest in personal or real property, shall not be invalid because of the absence of consideration, provided that the agreement changing, modifying or discharging such contract, obligation, lease, mortgage or security interest, shall be in writing and signed by the party against whom it is sought to enforce the change, modification or discharge." (L. 1936, c. 281, § 1, amending section 33(2) of the Personal Property Law.)*

The Circuit Court of Appeals refused to consider what law was applicable and refused to determine the applicability of New York law or of the New York statute, because these had not been called to the attention of the

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* This section was amended by L. 1944, c. 588, § 5, which added at the end thereof "or by his agent", the purpose of such amendment being to make clear that the writing required might be signed by the agent of the party to be charged, thus making the wording similar to that of the statute of frauds. 1944 Leg. Doc. No. 65(E); 1944 Report, Recommendations and Studies, pp. 714-719.

District Court. We here quote the following paragraph from its opinion:

> "We address ourselves first to a point which appears only in the trustees' reply brief on this appeal in answer to an argument in the 'R. F. C.'s' brief that the law of New York does not recognize the doctrine of 'promissory estoppel,' on which the trustees rely. They invoke an amendment to § 33, subd. 2 of the New York Personal Property Law, Consol. Laws, c. 41, made in 1936, under which 'an agreement * * * to discharge in whole or in part, any contract * * * shall not be invalid because of the absence of consideration,' if it is in writing and signed by the party. They argue that since the notes were made in New York and were payable there, the validity of the promise to discharge a part of the interest must be judged by the law of that state, and that Mr. Jones's letter satisfied the conditions prescribed in the section, although the promise was not made in New York. *We refuse to decide this question, for, although it is true that we may affirm a judgment upon grounds not urged in the lower court, we may not reverse one upon such a ground.* (*Virtue* v. *Creamery Package Co.*, 227 U. S. 8, 38, 33 S. Ct. 202, 57 L. Ed. 393; *Becker Co.* v. *Cummings*, 296 U. S. 74, 80, 56 S. Ct. 15, 80 L. Ed. 54; *General Utilities Co.* v. *Helvering*, 296 U. S. 200, 206, 56 S. Ct. 185, 80 L. Ed. 154; *Helvering* v. *Tex-Penn Co.*, 300 U. S. 481, 498, 57 S. Ct. 569, 81 L. Ed. 755; *Hormel* v. *Helvering*, 312 U. S. 552, 556, 61 S. Ct. 719, 85 L. Ed. 1037; *Libbey-Owens-Ford Glass Co.* v. *Sylvania Industrial Corp.*, 2 Cir., 154 F. 2d 814, 816.) This is particularly apposite in the case of an argument raised for the first time after the appellee has filed its brief, which it has had no chance to answer. Whether the point will be open in the district court after this appeal, we do not say; nor do we indicate any opinion on the merits."

The grave error involved in this quoted paragraph, particularly in the words that we have italicised, is obvious.

A. Cases in the Supreme Court.

Hormel v. *Helvering*, 312 U. S. 552, and *Helvering* v. *Richter*, 312 U. S. 561, argued and decided together, March 17, 1941.

In these two cases, an applicable statute had been wholly overlooked in proceedings before the Board of Tax Appeals. The *Hormel* decision was appealed to the Circuit Court of Appeals, Eighth Circuit; and that Court, contrary to the decision of the Circuit Court of Appeals in the present case, reversed the decision below by reason of the overlooked statute. This reversal was sustained by the Supreme Court, on certiorari. A similar decision of the Board of Tax Appeals in the *Richter* case was appealed to the Circuit Court of Appeals, Third Circuit; and that Court refused to consider the overlooked statute and affirmed the decision below. This refusal to reverse and to apply the overlooked statute was itself reversed by the Supreme Court, on certiorari.

In the present case, the Circuit Court of Appeals has erroneously refused to do what the 8th Circuit did in the *Hormel* case, with the approval of the Supreme Court; and it has erroneously done exactly what the 3rd Circuit in the *Richter* case was reversed for doing. The decisions of the Supreme Court in these two cases were made by a unanimous Court.

No better review of the law to be applied can be found than in the opinion of Mr. Justice Black in the *Hormel* case, large parts of which are printed in the Appendix hereto. The general rule of appellate procedure, one that is often stated in varying forms, is properly applicable when the point or argument raised on appeal is one that

might have been obviated below if it had been raised there—usually by additional evidence, by amendments, or by some correction of the procedure. New issues of fact are not to be litigated on appeal. Seldom should a matter be considered on appeal on behalf of a party who has intentionally waived it in the Court below. But the opinion in the *Hormel* case makes it perfectly clear that this general rule is not applicable with respect to decisive matters that could not have been obviated below, especially overlooked statutes. Moreover, even though the error is one that might have been obviated below, this Court and other Courts have often reversed a judgment and remanded the case for new determination as justice requires.

There is no substantial distinction between the *Hormel* and *Richter* cases and the present one. This Court and the Circuit Court of Appeals have no less power to review, reverse, or correct the orders of the District Court, sitting as an Administrative tribunal in Bankruptcy, than was expressly conferred by statute with respect to decisions by the Board of Tax Appeals. In those cases, the overlooked statute was a Federal statute; in the present case it is a State statute, one of which the Court was bound to take judicial notice and to apply in accordance with the ruling in *Erie R. Co.* v. *Tompkins,* 304 U. S. 64 (1938).

This Court said in the *Hormel* case: "Whether articulated or not, the philosophy underlying the exceptions to the general practice is in accord with the statutory authority given to courts reviewing decisions of the Board of Tax Appeals—decisions not in accordance with law should be modified, reversed or reversed and remanded 'as justice may require' ".

In the *Hormel* opinion, two of the other cases cited by the Circuit Court of Appeals as authority for its deci-

sion are expressly distinguished. The Court said: "In *Helvering* v. *Tex-Penn Oil Co.*, 300 U. S. 481, 498, 57 S. Ct. 569, 577, this Court declined to consider a newly presented question, but pointed out that it had not been raised by the Commissioner either in his notice of tax deficiency, in his appearances before the Board of Tax Appeals or the Circuit Court of Appeals, or in his petition for certiorari to this Court. And in *General Utilities & Operating Co.* v. *Helvering*, 296 U. S. 200, 206-207, 56 S. Ct. 185, 187, though this Court said that the Circuit Court of Appeals should not have considered a contention not presented to or ruled upon by the Board of Tax Appeals, the statement was buttressed by adding that the Circuit Court of Appeals had 'made an inference of fact directly in the conflict with the stipulation of the parties and the findings, for which we think the record affords no support whatever'."

The other three cases cited by the Court below are much more easily distinguishable, either as hardly in point at all or as involving a matter that might have been obviated had it been raised below. When writing the *Hormel* opinion, this Court felt no need for distinguishing them.

The following cases support the *Hormel* and *Richter* decisions:

Lilly v. *Grand Trunk W. R. Co.*, 317 U. S. 481 (1943). In a suit based upon the Federal Employers' Liability Act, the Courts of Illinois had entered and sustained a judgment for the defendant. This action was unanimously reversed by the United States Supreme Court. In an opinion by Mr. Justice Murphy, the Court said: "Respondent insists that reliance cannot be placed on Rule 153 [of the Interstate Commerce Commission] because it was not called to the attention of the trial court or the jury. . . . We do not regard this point as well taken. . . . The failure of petitioner's counsel to call Rule 153 to the attention of the trial court should no more deprive

petitioner of its benefits than the failure to plead specifically the Federal Employers' Liability Act foreclosed the application of that Act on appeal to test the correctness of the trial judge's refusal to charge in *Grand Trunk Western R. Co.* v. *Lindsay*, 233 U. S. 42."

Pecheur Lozenge Co. v. *Nat'l Candy Co.*, 315 U. S. 666 (1942). A suit for trademark infringement was brought "under the Trademark Laws of the United States". The District Court entered a decree for the plaintiff and this was reversed by the Circuit Court of Appeals. In a *per curiam* opinion the Supreme Court said: "Both courts below having failed to consider or apply local law, we granted certiorari . . . in order to determine whether local law or federal law should have been applied in a suit for infringement of a trademark registered under the Trademark Act of 1905, . . . and we requested counsel to 'present their views as to whether state law governs and, if so, what the applicable state law is.' The opinions below, the printed record and the petition for certiorari give no indication that the suit was not founded upon a trademark registered under the 1905 Act, as the bill of complaint had made it appear. But an examination of the original exhibits, not printed in the record, and of petitioner's brief on the merits here, discloses that the registration referred to is that of petitioner's labels under the Copyright Law of the United States, and not registration under the Trademark Law. It thus appears that petitioner has alleged no cause of action under the Copyright Law and is not entitled to the benefits of registration under the Trademark Law. The only cause of action that this record could possibly support is for unfair competition and common law 'trademark infringement', to which local law applies." The decree was vacated and the cause remanded to the Circuit Court of Appeals to afford it opportunity to apply the appropriate local law and for further proceedings.

Murdock v. *Ward,* 178 U. S. 139 (1900). A taxpayer sued to recover taxes illegally collected, asserting the invalidity of a taxing statute. This Court held the statute to be valid. However, it further held that on its proper interpretation the statute did not apply to legacies under $10,000, a point not raised below. The Court said: "We here meet the formal difficulty that neither the complaint in the circuit court nor the assignments of error in this court apparently questioned the correctness of the construction put upon the statute by the collector. The questions raised and considered only involved the validity of the act, and not its construction if valid. As, however, the parties proceeded on a mutual mistake of law, we think the practical injustice that might result from an affirmance of the judgment may be avoided by *reversing the judgment* at the cost of the plaintiff in error, and sending the cause back to the circuit court, with directions to proceed therein according to law."

In the present case there is no reason for charging your petitioner with costs.

Fourth Nat. Bank v. *Francklyn,* 120 U. S. 747, 751 (1887). The liability of a stockholder for corporate debts under certain statutes of Rhode Island was involved. In the Courts below another statute of partial repeal was overlooked. The Court, by Mr. Justice Gray, said: "It is contended for the defendant that this court should not review a judgment on a ground which was not presented in the court below. That is doubtless the general rule. . . . But it would be unreasonable to apply it when the effect would be to make the rights of the parties depend upon a statute which, as we know, and are judicially bound to know, is not the statute that governs the case." In this case the overlooked statute was found not to require a reversal.

B. Cases in the Circuit Court of Appeals Supporting the Decisions and the Reasoning of This Court in the Above Cases.

Joint Council v. *D. L. & W. R. Co.*, 157 F. 2d 417 (1946, *Second* Circuit); the Court raised a new point *sua sponte*, ordered new briefs, and reversed. In its decision in the present case, the Second Circuit is inconsistent with itself.

U. S. v. *Certain Parcels of Land*, 144 F. 2d 626 (1944, 3rd Circuit); the case had been tried on the theory that Pennsylvania law was controlling, no other authorities being cited—reversed and remanded.

Helvering v. *Rubinstein*, 124 F. 2d 969 (1942, 8th Circuit); reasoning of Hormel case approved, but decision affirmed and remanded with directions to permit application to reopen the case.

American Legion v. *First N. Bank*, 113 F. 2d 868 (1940, *Second* Circuit); judgment below reversed, on the basis of a Regulation of the Federal Reserve Board not called to attention of Court below.

Thompson v. *Hocking V. R. Co.*, 45 F. 2d 155 (1930, 6th Circuit); negligence case brought under Federal Employers' Liability Act, reversed and remanded because action might be sustained under Boiler Inspection Act, not called to attention of either the District Court or the Appellate Court.

C. Cases in the State Courts Fully Supporting the Above Federal Cases.

Cunningham v. *Cunningham*, 72 Conn. 157, 44 A. 41 (1899), reversing because of an overlooked statute, followed in numerous other cases as recently as 1942.

Rosenthal v. *Liss,* 269 Mass. 373, 169 N. E. 142 (1929), reversed because the Court applied a statute not yet operative when the cause arose, although that fact had not been called to the attention of either Court by counsel.

Beekman v. *Frost,* 18 Johns. (N. Y.) 544 (1820, Court of Errors), opinion by Spencer, *C. J.,* similar to that in *Hormel* case, never disapproved since.

Cappon v. *O'Day,* 165 Wis. 486, 162 N. W. 655 (1917), opinion by Rosenberry, *J.,* reversing because *a fact of record,* decisive of the case, was overlooked below.

People v. *Schlaeger,* 391 Ill. 314, 63 N. E. 2d 382 (1945); general rule "has no application to legal defenses based on public statutes".

White v. *Moore,* 288 Pa. 411, 136 A. 218 (1927); "some basic or fundamental error seriously affecting the merits of the case", but raised for the first time on appeal.

Cases stating and applying the general rule are very numerous. In most such cases it appears that the point raised on appeal might have been obviated if raised below, that it has been intentionally waived, or that the delay in raising it was intentional.

D. English Cases in Accord With *Hormel* v. *Helvering.*

Glebe Sugar Ref. Co. v. *Trustees* [1921], 2 A. C. 66, in the House of Lords. "After the appeal had been fully argued and judgment had been reserved", Lord Atkinson called the attention of the other Lords to a statute until then wholly overlooked. The House ordered a reargument and reversed the judgment of the trial court and the affirmance thereof by the Court of Session (Scot.).

Benaim & Co. v. *Debono* [1924], A. C. 514, in the Privy Council. Sales contract made in Malta, to be performed

at Gibraltar. Judgment for plaintiff in Commercial Court of Malta, affirmed by the Malta Court of Appeals, applying the Civil Law of Malta, was reversed and the case dismissed in accordance with a provision of the Sales Act of Gibraltar never called to the attention of the Malta Courts. The law of the place of performance governed, not the law of the place of making.

E. The Question of New York Law Was First Raised by Counsel for RFC, Not by Counsel for Petitioner.

The applicability of New York law having been properly and correctly raised on appeal by counsel for RFC, counsel for the petitioner were bound to meet the issue so raised. Even if they were "surprised", they could not avoid the issue on such a ground.

The issue thus raised is the issue as to whether New York law is the applicable law and as to what that law is. It is obvious that in determining this issue the statutes of New York are not to be segregated and disregarded. It is equally obvious that counsel for neither side can properly allege "surprise" or lack of opportunity for research and argument, as a reason for the Court's refusal to determine and to apply the properly applicable law. It is true that the specific New York statute was first called to the attention of the Court in the appellant's reply brief; but this was in meeting the issue as to New York law raised on behalf of the appellee, the RFC. It betrays great confusion as to the facts when the Court says that this is "an argument raised for the first time after the appellee has filed its brief, which it has had no chance to answer". The issue of New York law was raised in the very brief that the appellee had filed. It had ample opportunity to examine the New York statutes, both before it asserted in its own brief the applicability of New York law and on the argument in the Circuit Court of Appeals. The difficulty was, not that it "had no chance to answer", but that *no answer was possible.*

POINT II.

Refusal to apply New York law is in conflict with the decision in *Erie R. Co.* v. *Tompkins*, 304 U. S. 64 (1938) and with the policy underlying that decision.

Since the decision in *Erie R. Co.* v. *Tompkins*, it was error to refuse to apply the law of New York. On the undisputed facts of record, that law was applicable; and there was no other system of law that could be applicable. No "federal general common law",—since this Court in the *Tompkins* case reversed the Second Circuit for applying such a non-existent system, as it believed the decision in *Swift* v. *Tyson* required.

In his tribute to Judge Swan, printed in 57 Yale L. J. 167, 170 (December, 1947), Judge Learned Hand says that the *Tompkins* case "involved a tort committed in Pennsylvania, whose common law on the point was different from the great body of decisions elsewhere. At first we were going to follow the Pennsylvania decisions for we did not know the others, and the briefs—as is so often the case—were inadequate. After much delving he [Judge Swan] found that, if we were to apply the 'general law'—as we were then bound to do in a 'diversity case'—the Pennsylvania rule did not govern; and so we held and were reversed by the epoch-making *volte face* of the Supreme Court."

Their decision was reversed, not because the Court, with "much delving", adopted a new "theory of the case" and applied a system of law not theretofore adequately presented, but *because it applied the wrong system.* Its decision should again be reversed in the present case and for the same reason. Again it has applied the wrong system and for wrong reasons—doubly wrong, because the reversal of its own decision in the *Tompkins* case required it to apply State law, and because the decisions in *Hormel*

v. *Helvering* and *Helvering* v. *Richter* have instructed it to apply the properly applicable statute law even though the statute was not called to the attention of the District Court.

In applying, however erroneously, the principles of a supposed "general common law", the District Court was quite unconscious of the fact that the rights of the parties are governed by the law of the State of New York, as well as of the fact that there is a specific New York statute applicable to the case. The Court was quite unaware that it was going *contra* to the rule in *Erie R. Co.* v. *Tompkins.*

In the Circuit Court of Appeals, however, both parties expressly asserted that the applicable law is the New York law; and the Court was definitely informed as to the statutory provision in that State. Yet, for reasons both factually and legally incorrect, it refused to determine either the applicability of State law or the applicability of the specific New York statute. The existence of the statute was not overlooked; but the Court failed to remember its own experience in *Erie R. Co.* v. *Tompkins* and made no reference to that case.

Both Courts alike were bound to take judicial notice of the New York law, including the particular statutory provision.

POINT III.

The decision of the Courts below is in conflict with Section 122 of the Uniform Negotiable Instruments Law, a rule directly derived from the law merchant and now a part of the statutory law of every American jurisdiction.

By the law merchant and the continental civil law of which it was a part, a negotiable note or bill could be discharged by its holder by a mere oral renunciation. *Foster* v. *Dawber,* 6 Ex. 839 (1851). This rule was perpetuated in the Negotiable Instruments Law, Sec. 122, except that the renunciation must be in writing. Neither seal nor consideration nor subsequent action in reliance is necessary. This Uniform Statute has long since been adopted in every State of this Union, and in the District of Columbia. Every Court in the land is bound to take judicial notice of it and to apply it in a proper case, even though it may have been overlooked and neither pleaded nor argued.

Thus in *Leary* v. *Citizens Bank,* 128 Conn. 475, 23 A. 2d 863 (1942), the trial Court gave judgment in favor of the holder of a check against the drawee bank, wholly overlooking a provision to the contrary in N. I. L. The Supreme Court promptly reversed. In *G. & H. Investment Co.* v. *Raymond,* 113 Conn. 778, 155 A. 497 (1931), in a suit by the holder against an indorser, the trial Court gave judgment for the defendant because of lack of notice of dishonor. The Court and counsel *all* overlooked a waiver of demand and notice printed on the face of the note. The Supreme Court reversed the decision, correcting the legal error caused by the factual ignorance.

If Sec. 122 of the N. I. L. is applicable to this case, will it be asserted that it is made inapplicable by being overlooked in the Courts below?

Section 122, N. I. L., is as follows:

> "The holder may expressly renounce his rights against any party to the instrument, before, at or after its maturity. An absolute and unconditional renunciation of his rights against the principal debtor made at or after the maturity of the instrument discharges the instrument. But a renunciation does not affect the rights of a holder in due course without notice. A renunciation must be in writing, unless the instrument is delivered up to the person primarily liable thereon."

Observe that the second sentence does not limit the operation of the first sentence in any respect. The first sentence empowers the holder to renounce his rights *against any party,* at any time. The second and third sentences provide for a *discharge of the instrument,* as against anybody except a "holder in due course". The second sentence is limited to renunciations of rights *against the principal debtor* made "at or after maturity"; a taker thereafter cannot be a holder in due course.

Under the first sentence of this Section, a written renunciation is not rendered ineffective by the fact that it is conditional. All that is necessary is that the condition shall be fulfilled before the renunciation can be pleaded as a final discharge. Prior to such fulfilment, the renunciation is binding and irrevocable, the condition being merely "suspensory". [A term used in the Louisiana Code and the Civil Law everywhere.]

In this respect a conditional release or other discharge is no different from a conditional promise. An executory promise is none the less binding and irrevocable by reason of its being subject to a condition precedent. Legal obligation exists from the formation of such a contract; it is only the *duty of immediate performance* that awaits fulfilment of the condition. Restatement, Contracts, §§ 250, 254.

"A release which states that it shall take effect on the occurrence of a condition precedent is operative as a discharge on the occurrence of the condition." Restatement, Contracts, § 404. Just as in the case of a conditional promise, the condition of a release is merely "suspensory", the delivered instrument being quite irrevocable in the meantime.

Renunciation of rights under the first sentence of Section 122, N. I. L., is not made inoperative by the fact that it is conditional or the fact that it applies to only a part of the debt. *Dickinson* v. *Vail,* 199 Mo. App. 458, 203 S. W. 635 (1918), renouncing right to part of the note against one maker if holder failed to prosecute action against a co-maker. The Court said: "The first sentence [of § 122] authorizes the holder of the note to renounce his rights against *any* party to the instrument; while the second sentence refers alone to the *principal* debtor, and makes 'an absolute and unconditional renunciation' as to him a discharge of the instrument. But this does not hinder such holder from conditionally releasing any of the parties to the note, including the principal debtor. The statute merely affirms the effect of an absolute and unconditional renunciation to the principal debtor, but it does not prevent a renunciation that is not absolute and unconditional."

A creditor promised his debtor in writing that this writing might be pleaded in defense if the creditor should bring suit within five years. The creditor so sued, fulfilling the condition. Plea sustained. *Gibbons* v. *Vouillon,* 8 C. B. 483 (1849).

In a suit on a promissory note, the defendant pleaded a written release. The plaintiff proved that this had been delivered to be a full discharge only in case of the debtor's bankruptcy. Since the condition had not been fulfilled, the plea was insufficient. *Stiebel* v. *Grosberg,* 202 N. Y. 266, 95 N. E. 692 (1911).

The renunciation by RFC of its right to 1 per cent interest was not the less effective by the fact that it was of no more than a fractional part or was conditional or was in promissory form. The condition of its final operation as a discharge was full payment of the claims of RFC in the reorganization, on the 4 per cent basis, a condition consisting of action by the Trustees and requiring no action or additional assent by RFC. That condition was performed up to the hilt—indeed, RFC received full payment of its claims on the 5 per cent basis, the final payment being under compulsion of the erroneous Court Order. The letter of Mr. Jones reserved no power in RFC to withdraw it or to control its operation. By both Sec. 122, N. I. L., and the special New York statute previously discussed, the letter of Mr. Jones was legally operative, according to its own terms, from the moment it was executed.

That a written renunciation under § 122, N. I. L. requires no consideration is not a debatable question.

In *McGlynn* v. *Granstrom*, 169 Minn. 164, 210 N. W. 892 (1926), the Court reviewed authorities and then said: "So we are constrained to hold that the renunciation, which under § 122 must be in writing, is one accomplished by the unilateral act of the holder. Ordinarily, if not always, it will be without consideration."

In Byles on Bills, 20th ed., p. 241 (1939), 17th ed., p. 252 (1911), it is said: "To this rule [generally requiring consideration] it has been repeatedly held that contracts on bills of exchange form an exception, and that the liability of the acceptor or other party, remote or immediate, though complete, may be discharged by an express renunciation of his claim on the part of the holder, without consideration. . . . Parties liable, who are expressly told that recourse will not, in any event, be had to them, are almost sure, in consequence, to alter their conduct and position."

This is quoted with approval in Daniel, Neg. Insts., 5th ed., § 542 (1905).

In order to be operative under § 122, N. I. L., it is not necessary that the writing signed by the creditor shall contain the word "renounce". The statutory words are: "The holder may expressly renounce his rights against any party to the instrument, before, at or after its maturity". It is the intention to renounce and not the mere form of its expression that is required by the statute. The intention may be variously expressed. Such terms as waive, release, discharge, surrender, and give up are certainly as effective as is the word renounce; and, as has been seen above, they are not rendered ineffective by the fact that their full effect is postponed till a future time, being made expressly conditional on a future event.

The express words in Mr. Jones' letter, December 21, 1938, are "this Corporation will accept 4 per cent from the date of bankruptcy in full settlement," having substantially the same form as he had used in several earlier letters. In spite of being worded in the future tense, these letters were regarded by RFC itself as conditional waivers.* A covenant not to sue is in promissory form; but it is not prevented thereby from operating as a discharge. "A covenant not to sue amounts in law to a release." Byles on Bills, 20th ed., p. 241 (1939), 17th ed., p. 252 (1911).

A contract of accord, whereby a creditor promises that he "will accept" a substituted performance in full satisfaction, is not prevented from being operative as an immediate suspension by the fact that it is in promissory

* Thus, in the letter dated September 28, 1936 (R., pp. 26-28), RFC wrote: "Nothing in this arrangement contained shall be construed as a waiver by the Reconstruction Finance Corporation of the right to claim interest at the rate of 5% per annum if all interest is not paid as aforesaid at the rate of 4% per annum." This language is repeated in the affidavit of Mr. Barriger, Chief Examiner of RFC, filed in Court by RFC with its Answer (R., pp. 74-76, fol. 227).

form and in the future tense. This is supported by Restatement, Contracts, § 417(a), quoted and approved in *Union Cent. L. Ins. Co.* v. *Imsland,* 91 F. 2d 365 (1937, C. C. A.), and *Milici* v. *Di Francesco,* 122 Conn. 267, 188 A. 884 (1936).* Specific performance of an accord executory was decreed in *Very* v. *Levy,* 13 How. (U. S.) 345 (1851). The New York decisions *contra* have been nullified by Sess. Laws N. Y. 1937, Ch. 77.

The letter of Mr. Jones, saying that "this Corporation will accept 4 per cent from the date of bankruptcy in full settlement" was conditional solely on specified action by the Trustees. No power of withdrawal was reserved; and the complete fulfilment of the prescribed condition required no action of any kind on the part of RFC.

POINT IV.

The legal operation of the original contract of loan and of its subsequent modification and partial discharge is determined by the law of the State of New York.

The only law that can properly be applied in this case is the law of the State of New York. The Circuit Court of Appeals expressly refused to decide this question, and refused to apply New York law.

The following statement of facts is quoted from an affidavit filed by RFC and printed in the record at page 58:

> "All of said loans were disbursed to the Debtor by Reconstruction, and all of said notes evidencing said loans were then and there delivered by the Debtor to Reconstruction, in the City of New York, New York. As appears by their terms, all of said notes are dated

* The often repeated rule to the contrary was a hang-over that dated from the 15th Century before the common law courts recognized a promise as a sufficient consideration for another promise.

in the City of New York, New York, and both the principal and interest thereof are payable to Reconstruction at the Federal Reserve Bank of New York. All items of collateral securing said notes . . . were duly assigned, pledged, and delivered by the Debtor to Reconstruction in the City of New York, State of New York."

Later, in the Brief for Appellee RFC in the Circuit Court of Appeals (p. 28), raising for the first time, for the advantage and in behalf of RFC, the question as to New York law, counsel made the following statement:

"The Debtor's notes which were delivered to the RFC in evidence of RFC's loans to the Debtor were all executed and delivered in the City of New York, State of New York, and they are all payable at the Federal Reserve Bank of New York in the City of New York. Reference is made to Exhibit B [printed in the Appendix to the Brief] which consists of a reproduction of relevant portions of the last remaining unpaid note of the Debtor evidencing a loan from the RFC. This note is typical with respect to the place of execution and delivery and the place of payment.

"From the foregoing facts it would seem clear that New York law should govern any question with respect to the payment of the RFC notes."

It was in reply to this assertion that counsel for the petitioner agreed and called attention to the New York statute.

The letter of Mr. Jesse Jones, December 21, 1938, was mailed in Washington, D. C. and received by the Trustees in New Haven, Conn. (R., pp. 229, 230). By its own terms, it was ancillary to the original loan, providing for no more than a modification and partial discharge of the debt so created. It was in form a promise to accept a reduced

amount in full satisfaction. By necessary implication, this amount was to be paid at the Federal Reserve Bank in New York, since it was the principal of the original loan and four-fifths of the original interest.

If, in making his promise, Mr. Jones was bargaining for payment by the Trustees in the course of the reorganization, to be accepted by their making such payment, the unilateral contract created thereby was made in New York; the payments so bargained for were in fact made there, including the final and excessive payment made by Court Order.

If the promise of Mr. Jones be regarded, not as a promise for a requested consideration, but merely as a conditional promise of modification and discharge, the condition so required was payment in New York, a condition that was in fact fully performed there.

In determining the law governing the legal effect of either the original contract of loan or the subsequent promise of Mr. Jones, we are not in the least embarrassed by the conflict in the laws by which the effect of other contracts is determined. In all jurisdictions known to Anglo-American jurisprudence, and by the rules laid down by all the writers on the Conflict of Laws, the rights and duties of your petitioner and of RFC are determined by the law of New York. On the facts of this case, the governing law is New York law. That this is so is well established by decisions of the United States Supreme Court, and by those of New York, Connecticut, the District of Columbia, other States and England.

Story, Confl. Laws, § 280, reads: "Where a contract is either expressly or tacitly to be performed in any other place [than the place of making] there the general rule is, in conformity to the presumed intention of the parties, that the contract as to its validity, nature, obligation, and interpretation, is to be governed by the law of the place of performance."

Earlier cases on which this was based are *Wayman* v. *Southard,* 10 Wheat. 1 (1825), by Marshall, *C.J.; Cox* v.

U. S., 6 Pet. 172 (1832); *Thompson* v. *Ketcham*, 8 Johns. (N. Y.) 146 (1811), by Kent, *C.J.*; *Robinson* v. *Bland*, 2 Burr. 1077, 1 W. Bl. 234, 256 (1760), by Lord Mansfield.

The leading case most closely parallel to the present one is *Pritchard* v. *Norton*, 106 U. S. 124 (1882), cited with approval in many subsequent cases in this Court, at least as recently as 1938. An indemnity bond was signed and delivered in New York. By the New York law, *lex loci contractus*, it was invalid for lack of consideration (the effect of a seal having been changed by statute). But this gratuitous bond was given to one who had bound himself as surety on an appeal bond, given and to be performed in Louisiana, and later performed there by payment of a judgment. It was in Louisiana that the payment required by the indemnity bond was to be performed; and in Louisiana the law required no consideration. The Court held that Louisiana law applied and enforced the gratuitous promise in the bond.

Cases in accord are: *Hall* v. *Cordell*, 142 U. S. 116 (1891); *London Assur.* v. *Companhia de M.*, 167 U. S. 149 (1897); *New York L. Ins. Co.* v. *Dodge*, 246 U. S. 357 (1918).

Connecticut: *Beggs* v. *Bartels*, 73 Conn. 132, 46 A. 874 (1900); *Chillingworth* v. *Eastern T. W. Co.*, 66 Conn. 306, 33 A. 1009 (1895).

District of Columbia: *Fisk Rubber Co.* v. *Muller*, 42 App. D. C. 49 (1914).

Other state decisions (selected from very many): *Manhattan L. Ins. Co.* v. *Johnson*, 188 N. Y. 108, 80 N. E. 658 (1907); *Old Dominion C. M. Co.* v. *Bigelow*, 203 Mass. 159, 174, 89 N. E. 193, 200 (1909); *Waverly N. Bank* v. *Hall*, 150 Pa. 466, 24 A. 665 (1892).

English cases: *Spurrier* v. *LaCloche* [1900] A. C. 446; *Benaim & Co.* v. *Debono* [1924] A. C. 514, where the Privy

Council reversed the Malta courts for failing to apply the statutory law of Gibraltar (place of performance) even though that law had not been called to their attention; the Malta courts had applied the civil law of Malta, where the contract had been made.

Of course, Dicey agrees; Confl. Laws, 529, ed. 2.

In the present case the contract of loan was made in New York and was in every respect to be performed there. The letter of Mr. Jones made no change in the place of performance. It seems that everywhere the law as to the effectiveness of a release or of a performance as a discharge is governed by the law of the place of performance even though the *lex loci contractus* may have been elsewhere. *Tarbox* v. *Childs*, 165 Mass. 408, 43 N. E. 124 (1896), contract of sale, payment to be made in New York; later the buyer gave his note payable in Massachusetts for the unpaid balance; whether this note operated as a mere suspension or as a discharge of the sale contract was determined by New York law.

Garfield Aniline Wks. v. *Zendle*, 43 F. 2d 537 (1930, C. C. A.); *York M. & A. Co.* v. *Cyclops Steel Co.*, 280 Pa. 585, 124 A. 752 (1924).

Beale, Confl. Laws, § 374.1, says: "Logically it must be said that the law of the place of performance of a contract determines whether it is discharged by a release".

The Courts Below Were Bound to Take Judicial Notice of the New York Law, Common and Statutory.

In order to make any determination of the legal effect of the transaction between these parties, it was necessary for the Court to determine the particular State whose law controlled that effect. Having determined it, the Court was then bound to take judicial notice of that law and to apply it to the facts. The State so selected is not a

jurisdiction foreign to the federal Court; it is not one whose law must be proved as a fact. *Lamar* v. *Micou*, 114 U. S. 218, 223 (1885), "bound to take judicial notice, without plea or proof"; *Owings* v. *Hull*, 9 Pet. (U. S.) 607, 624 (1835).

The federal District Court, whether in a reorganization proceeding or in a commercial case within its jurisdiction, has no contract law of its own. It is a Court of the United States required to apply, in a domestic transaction like the present one, not some general federal law but the law of the particular State where performance is required. That, and no other, is the law of its forum.

When rendering its decision in this case, the District Court was sitting within the boundaries of Connecticut; but it was sitting as an Administrative Court in Bankruptcy in accordance with Acts of Congress. The undisputed facts of record show that all performances to be rendered by either party, whether of promises or conditions, were to be rendered in New York, with the result that it would be error to apply any other law than that of New York.

If it be argued that the law of Connecticut was applicable, because the District Court was sitting in that State, even though it was sitting as an Administrative Court in a reorganization proceeding under the Federal Bankruptcy statutes, the decision below is still erroneous and for the same reasons. In applying Connecticut law, the District Court must not exclude the Connecticut rules applicable where laws conflict. *Klaxon Co.* v. *Stentor Electric Mfg. Co.*, 313 U. S. 487 (1941). It must apply the law that the Connecticut Court would apply to the facts of record *in this case*; that is, to a contract made and to be performed in New York, not the law that the Connecticut Court would apply to a wholly domestic contract. To the facts of the case before this Court, the Connecticut Supreme Court of Errors would apply the law of New York. See cases cited, *supra*.

POINT V.

The decision of the Courts below is erroneous, even regarding it as based upon some system of general common law and equity, or upon such a system of New York or any other State. Before any withdrawal or denial of the validity of Mr. Jesse Jones' promise, the final cash payment required by him was on the verge of performance; and that final payment was in fact received by RFC within the time limit.

The promise made December 21, 1938, was expressly conditional on full payment of the claims of RFC, with interest at 4 per cent, in the course of reorganization. Such payment required action by the Trustees, action that they were under no legal duty to take. Their duty as trustees was merely to conserve and distribute assets according to law and as the Court might order. In order to fulfil the condition of the promised reduction, the Trustees petitioned the Court at least five times for permission to sell parts of the hypothecated securities and to pay the proceeds to RFC, and on two other occasions to pay to RFC the proceeds of sales of other property, always with the knowledge and consent of RFC; and they also voluntarily made available to RFC additional amounts by declaring dividends on certain stock owned and held by them, the Trustees having agreed that RFC should receive 70% of any dividends that might be so declared. The money so paid over to RFC amounted to nearly four million dollars. Although the lien of RFC on the securities and other property covered by the Trustees' petitions was superior to the claims of other creditors, those creditors had an equity in them and were entitled to protection by the Trustees and the Court. Their equity would be increased by the exact amount of the reduction in interest promised by RFC.

In making this promise of December 21, 1938, was Mr. Jones bargaining for full payment of the claims by the

Trustees in course of reorganization, so that the making of such payment would constitute a consideration (as defined in Restatement, Contracts, § 75)? This can not be answered with certainty, although there is cogent evidence that Mr. Jones desired the acceleration of final payment of the debt. It appears that RFC was aware that payment of its claim could "be substantially accelerated by the orderly sale of non-system collateral" (R., p. 128); and it gave as "a good instance" the 94,000 square feet of Park Square (Boston) real estate included in the collateral (R., p. 127). Among other sales of collateral subsequently negotiated and effected by the Trustees was this Park Square real estate (R., pp. 204-208, 217-221).

Full payment with interest at 4 per cent would benefit RFC; but we may assume that Mr. Jones was also moved by a desire to aid in the reorganization. If he bargained for it, RFC received it. RFC did not have to look solely to income from its collateral for repayment, and it did not have to wait for the distribution under the reorganization plan finally adopted. The cash payments made by the Trustees, augmented by the income on collateral applied by RFC to current interest (at 5 per cent) and to principal,* so far reduced the debt that on July 11, 1946, the Trustees petitioned the Court to permit the final payment out of general assets (R., p. 222). [In its Answer, filed Aug. 2, 1946, at the hearing on this petition, RFC repudiated the promise—R., p. 233.]

If, on the other hand, Mr. Jones did not bargain for full payment by the Trustees as a consideration, he nevertheless stated it as an express condition of the promise. The fulfilment of the condition required substantial action by the Trustees, as Mr. Jones was aware. From time to

* Part of this income amounting to more than $1,800,000 was made available to RFC by the voluntary action of the Trustees in declaring dividends on The Connecticut Company's Class B stock owned and held by the Trustees. This stock was not even a part of the hypothecated collateral; but the Trustees had agreed that RFC should receive 70% of any dividends that might be declared (R., pp. 117, 121).

time they took that action, Mr. Jones always being aware thereof. They made large payments in this process; and RFC received them and benefited thereby (R., pp. 194-221). On August 2, 1946, RFC refused to receive the payment that would have completed fulfilment of the condition; by April 30, 1947, RFC itself caused such complete fulfilment by application of income from collateral.

Prior to August 2, 1946, no attempt to withdraw the promise of Mr. Jones was made by RFC (R., p. 247). It was then too late to withdraw (wholly apart from the New York statute and sec. 122, N. I. L.). The substantial action and change of position by the Trustees had made the promise irrevocable and binding (subject to complete performance of the condition within the specified time). It had become binding either (1) because the Trustees had performed and RFC had received a large part of the bargained-for consideration, or (2) because of the substantial action and change of position by the Trustees in reliance.

A. Effect of Action by the Trustees as a Bargained-for Consideration.

Restatement, Contracts, sec. 45, reads as follows:

"*Revocation of Offer for Unilateral Contract; Effect of Part Performance or Tender.* If an offer for a unilateral contract is made, and part of the consideration requested in the offer is given or tendered by the offeree in response thereto, the offeror is bound by a contract, the duty of immediate performance of which is conditional on the full consideration being given or tendered within the time stated in the offer, or, if no time is stated therein, within a reasonable time."

Comment *b* reads thus: "Tender, however, is sufficient. Though not the equivalent of performance, nevertheless it is obviously unjust to allow so late withdrawal. There can be no actionable duty on the part of the offeror until he has received all that he demanded, or until the condition is excused by his own prevention of performance by

refusing a tender; but he may become bound at an earlier day. The main offer includes as a subsidiary promise, necessarily implied, that if part of the requested performance is given, the offeror will not revoke his offer, and that if tender is made it will be accepted. Part performance or tender may thus furnish consideration for the subsidiary promises. Moreover, merely acting in justifiable reliance on an offer may in some cases serve as sufficient reason for making a promise binding (see §90)."

No statement found in the law of contract is more reasonable and just than this. No case can be found to which this statement of law is more fully applicable than the case of the petitioner.

The Trustees rendered many and beneficial part performances. On July 11, 1946, they asked a Court Order for the final payment of the balance. All this was within the time stated by Mr. Jones—in the course of reorganization. Only on August 2, 1946, did RFC attempt to withdraw—"it is obviously unjust to allow so late withdrawal." By its repudiation on that date, RFC itself prevented complete fulfilment by the Trustees, so that "the condition was excused by its own prevention". But it had "become bound at an earlier day".

Moreover, RFC itself caused complete fulfilment of the condition within the time specified by Mr. Jones. It did this by applying the ample income from collateral on account of the claims. These claims, with interest at 4 per cent, were extinguished in full by April 30, 1947, as required by Mr. Jones. As final reorganization approached, the income from collateral kept piling up, so that when the Trustees made final payment of $433,456, as compelled by an erroneous order of the Court, and still in course of reorganization, RFC had received payment of its claims in full with an additional 1 per cent interest on unpaid balances from October 23, 1935 to January 1, 1945. The erroneous order should be reversed and repayment of all excess payments decreed.

B. Promise Binding Because of Action by Trustees in Reasonable Reliance.

Restatement, Contracts, sec. 90, reads as follows: "*Promise Reasonably Inducing Definite and Substantial Action.* A promise which the promisor should reasonably expect to induce action or forbearance of a definite and substantial character on the part of the promisee and which does induce such action or forbearance is binding if injustice can be avoided only by enforcement of the promise."

Did not Mr. Jones have "reason to expect" exactly what happened—prior to August 2, 1946? Was not the action or forbearance by the Trustees "definite and substantial"? Did not the promise "induce such action or forbearance"? Can "injustice be avoided" otherwise than by restitution of the compulsory overpayment?

Action or forbearance in reliance on a promise in accordance with this section is not called a "consideration" by the Restatement; but for some centuries prior to the issuance of that document it had been called "consideration" by the courts. In the very early history of Assumpsit, promises were enforced solely because of action or forbearance in reliance on them to the injury of the promisee. In recent times, decisions of this kind were sometimes explained as based upon an "estoppel theory of consideration". This was after Mr. Justice Holmes had distinguished between something bargained for by a promisor and subsequent action or forbearance by the promisee in reliance. He did not deny the efficacy of the latter. Instead, he said this: "There must be some ground for saying that the acts done in reliance upon the promise were contemplated by the form of the transaction either impliedly or in terms as the conventional inducement, motive and equivalent for the promise. But courts have gone very great lengths in discovering the implication of such an equivalence, sometimes perhaps even having found

it in matters which would seem to be no more than conditions or natural consequences of the promise." *Martin* v. *Meles*, 179 Mass. 114, 117, 60 N. E. 397 (1901).

So far, indeed, had the courts gone, from the early history of Assumpsit down to the present, that the learned reporter Samuel Williston and his advisers felt bound to present Sec. 90 as a statement of the existing law. Of course, the action or forbearance held sufficient had occurred in many forms.

Among the many antecedent cases on which Section 90 is based are those found in the following classes, many of them being cases in which the Court did not determine whether the action or forbearance in reliance was bargained for or not, and many others (found in each class) being cases in which it is perfectly clear that the action or forbearance in reliance was not bargained for:

(a) forbearance by debtor to pay as agreed, in reliance on promise by a creditor to extend the time of payment or to refrain from exercising a power of acceleration, *In re Barbara Campbell*, 105 F. 2d 197 (1939, C. C. A. 9th), cert. den. 308 U. S. 593, stated at some length in the Appendix, almost on all fours with the present case;

(b) forbearance by debtor to take steps to redeem or to protect his interest otherwise, in reliance on mortgagee's promise not to foreclose or to act for debtor's benefit, *Schroeder* v. *Young*, 161 U. S. 334 (1896), mortgagor "lulled into a false security"; *Firestone* v. *Miroth Const. Co.*, 215 App. Div. 564, 214 N. Y. S. 239 (1926), "contrary to equity and good conscience" to permit foreclosure;

(c) forbearance by creditor to bring suit in reliance on debtor's promise not to plead statute of limitations or to deposit further security, *U. S.* v. *Curtiss Aeroplane Co.*, 147 F. 2d 639 (1945, C. C. A. 2d); *Alliance Bank* v. *Broom*, 2 Drew. & S. 289 (1864);

(d) gratuitous promissory note given to a bank, with action in reliance thereon by the bank and its customers (often, but not always, involving fraud), *Deitrick* v. *Greaney*, 309 U. S. 190 (1940); *First N. Bank* v. *Sagerson*, 283 Pa. 406, 129 A. 333 (1925);

(e) action by a promisee in reliance on a gratuitous promise of a gift conveyance of land, *Freeman* v. *Freeman*, 43 N. Y. 34 (1870);

(f) expenditures in reliance on a gratuitous promise of a license for use of land, *Rerick* v. *Kern*, 14 S. & R. 267 (1826, Pa.);

(g) promises by an owner to pay a commission for a completed sale, but repudiated and sale prevented after the broker's action in advertising and soliciting, *Braniff* v. *Baier*, 101 Kan. 117, 165 P. 816 (1917);

(h) promises of charitable or business subscriptions followed by changes of position by the promisee, *Allegheny College* v. *Nat. Chautauqua Bank*, 246 N. Y. 369, 159 N. E. 173, 57 A. L. R. 980 (1927);

(i) promises by a gratuitous bailee to keep property insured, *Siegel* v. *Spear & Co.*, 234 N. Y. 479, 138 N. E. 414, 26 A. L. R. 1205 (1923);

(j) gratuitous promise by a bank to make due collection of a note left with it in reliance, *Robinson* v. *Threadgill*, 35 N. C. (13 Ired.) 39 (1851).

Section 90 was approved by the Council of the Institute and adopted by its members, as a statement of existing law, not as new legislation. Since its publication it has been approved and applied in scores of jurisdictions.

The action and forbearance by the Trustees amply fulfil the requirements of the rule stated in Section 90. They include the following: Seven or more payments on account, out of proceeds of special sales, amounting to nearly $2,000,000 after obtaining special Court Order by

petition (R., pp. 194-221). More than $1,800,000 made available to RFC by the declaration of dividends. Forbearance to make any effort to refinance the debt at a rate lower than 5 per cent (R., pp. 238-240). Surely, these are "substantial and definite". Was this action or forbearance such as RFC "should reasonably expect"? The action (petitions, sales, and payments) was in pursuance of the express condition of the promise of December 21, 1938. The forbearance to attempt refinancing was not expressly referred to; but many a creditor's promise to his debtor has been enforced because the debtor was "lulled into security" and forbore to act for his own protection.

A reading of the memorandum of opinion in the District Court clearly shows that the seven large cash payments made by the Trustees were wholly overlooked by the Court, although they had been made by the Court's order, and that the Court was also unaware of the Trustees' dividend declarations. "I neither recall nor can I find record of any contemporary suggestions from any source that these debts should be paid off in cash." Also, "Thereafter there was no material change in the background" (R., p. 253).

At the time of writing this opinion, the Court may have supposed that the great reductions in the debt had come wholly from the income on collateral, whereas nearly $2,000,000 had come from the sales of collateral by the Trustees, collateral in which other creditors besides RFC had an equity, collateral that could not lawfully have been sold without an order of Court on a finding of benefit to the estate.

It is highly probable that after December 21, 1938, the Trustees did not affirmatively consider a refinancing of the entire loan with another creditor; this was because of the promise of Mr. Jones that the debt would be treated as a 4 per cent debt retroactively. Instead, they were caused to consider paying it off in cash during reorganization, if they could not induce RFC to waive the

condition of full payment by that time. They were caused to forbear to refinance with others, because they had already secured favorable terms from RFC itself.

The District Court thought of difficulties in the way of refinancing the total debt with a new creditor, possibly involving changes in the Plan of the Reorganization; and it failed to think of the fact that the loan was being paid off in cash, in accordance with its own orders, and without affecting the Plan except by reduction of the indebtedness of the estate.

It is far from improbable that a refinancing of the entire loan with another creditor could have been consummated. The collateral hypothecated with RFC was ample for such a purpose (cf. R., pp. 128, 246); and all the authorities involved would surely have been willing to cooperate for the benefit of the estate. But even if the attempt would have been unsuccessful, forbearance to make it is not thereby made insufficient as a consideration or as reliance.

That the Trustees did in fact forbear to refinance, and that they did in fact make cash payments of nearly $2,000,000 and petition for permission to pay the balance in cash, are matters of record. Payment in full during reorganization was an express condition of the promise made to them. It is a plain and ordinary inference from these facts that the action and forbearance by the Trustees were induced by this promise.

Courts have not hesitated to draw reasonable inferences in the light of human experience. This problem was before the Court in *Martin* v. *Meles,* cited above. Mr. Justice Holmes said: "It is true that it is urged that the acts of the committee [to whom the defendant had promised a subscription] would have been done whether the defendants had promised or not, and therefore lose their competence as consideration because they cannot be said to have been done in reliance upon the promise. But that is a speculation upon which courts do not enter. When an

act has been done [*i. e.*, a promise made], to the knowledge of another party, which purports expressly to invite certain conduct on his part, and that conduct on his part follows, it is only under exceptional and peculiar circumstances that it will be inquired how far the act in truth was the motive for the conduct, whether in the case of consideration . . . or of fraud." In the present case the circumstances are neither exceptional nor peculiar.

The Circuit Court of Appeals, after summarily disposing of the question of State law and of the New York statute, follows the opinion rendered in the District Court with respect to "promissory estoppel". It had before it the Transcript of Record that is now before the Supreme Court, but without the chronological outline of events given in this brief. It summarily disposes of "the whole notion of promissory estoppel" as a mere "afterthought". It even more briefly disposes of the action of the Trustees in making cash payments, either as a "consideration" or as fulfilment of the condition required by Mr. Jones.

The Court says: "The letter admits of no such interpretation, even though the condition was also a consideration: it did not ask for efforts by the trustees; it required that the loans should be 'fully paid.' It is impossible to torture those words into an effort to do the best one could, when one could." This striking phraseology shows that it is quite possible to torture the words of Mr. Jones' into something that they are not. He plainly asked for nothing more than full payment in course of reorganization; he got exactly that. His words are: "if, in the reorganization . . . the claims of this Corporation have been fully paid, this Corporation will accept 4 per cent from the date of the bankruptcy in full settlement of interest, regardless of the rate named in the face of the note."

From the Court's statement, it would be supposed by an ordinary reader that the "efforts" of the Trustees had been *futile*. He could hardly guess that RFC had actually received in cash all but a comparatively small balance before July 11, 1946; that this balance would have

been paid in cash soon after that date if RFC had not prevented it; that this balance was actually paid by April 30, 1947; and that by the close of the reorganization RFC had received in cash the full principal of the debt with interest at 5 per cent, being more than $800,000 in excess of what Mr. Jones had required.

A consideration of the rules of law above discussed, and of their application to the long series of letters and promises and actions in this case, demonstrates the sound reasons underlying the New York statute as to the modification and discharge of contracts and also Section 122 of the N. I. L. Renunciations and promises of modification and discharge always affect the state of mind of the obligor and induce action or forbearance by him in reasonable reliance; yet even in his own mind he may not analyze or separate the motivating elements of his own conduct. When questioned, he may not be able to say what he would have done but for the renunciation or promise. Section 122 of the N. I. L. is everywhere the law as to bills and notes. The New York statute extends the rule to all other kinds of contracts. Its extension by judicial action without the aid of statute is in process.

C. The Letters of the Trustees Nowhere Indicate That They Did Not Continually Rely on the Promised Reduction.

A careful reading of the correspondence appearing in the record will show that the letters of the Trustees to the Chairman of RFC, dated January 29, 1945 (R., p. 230), and thereafter (R., pp. 224, 225), were seriously misinterpreted by the Circuit Court of Appeals. Of course, under the New York statute and the N. I. L., Mr. Jones' promise was binding, wholly without regard to a consideration for it or action in reliance upon it. But

it is most unjust to misinterpret the letters and the attitude of the Trustees.

For a long period, RFC had actually accepted 4 per cent in lieu of 5 as provided in the notes (R., p. 222). A period then ensued in which there was some doubt as to whether the collateral would be sufficient to assure full payment of the debt; and the right of RFC to collect and apply the entire income from the collateral was in litigation (R., pp. 122-126).

On March 14, 1936, Counsel for the Trustees wrote asking whether RFC intended "to apply the payments received and expected to be received from collateral to the payment of interest at the rate of 4% or 5% and . . . to retain any income from collateral in excess of the interest on the notes" (R., p. 71).

On March 21, 1936, Mr. Jones replied that if the income so received (with any other payments that might be made by the Debtor) "is sufficient to pay interest in full in cash to date and continues sufficient to pay interest currently . . . this Corporation will accept 4 per cent in full settlement of the interest regardless of the rate named in the face of the note. If the income from the pledged collateral is greater than such past due and current interest at 4 per cent, the excess will be applied by this Corporation to the reduction of the principal amount of the indebtedness" (R., p. 72).

On April 4, 1936, Counsel for the Trustees wrote "I have not challenged the right of the Corporation to the collateral income and, as at present advised, have no grounds on which to base such a challenge" (R., p. 73).

On September 28, 1936, in a letter used by the Trustees in their petition for Court Order No. 102 (R., pp. 26-28), Mr. Jones wrote: "Nothing in this arrangement contained shall be construed as a waiver by the Reconstruction Finance Corporation of the right to claim interest at the rate of 5 per cent per annum if all interest is not paid as aforesaid at the rate of 4 per cent per annum."

At this time income from collateral was being held "in

escrow" pending court decision (R., p. 124). After Court Order No. 102 had authorized RFC to apply all collateral income to interest "at a rate not in excess of 5 per cent" and balance to principal (R., p. 104), on November 10, 1938, the Trustees wrote that although "interest . . . has been running at the rate of 5%" the income from collateral had been more than sufficient to pay it, with a balance for reducing principal; also that income was certain to remain more than sufficient. Therefore they "earnestly request that the rate on these notes be reduced to 4% as of November 1, 1938" (R., p. 228).

This was a request that from November 1, 1938, the income from collateral should be immediately and currently applied to interest at 4 per cent instead of 5 per cent, leaving a proportionately larger balance for diminishing the principal of the debt. That Mr. Jones so understood it is certain; for in his reply of December 21, 1938, he repeats in almost exact terms his earlier promises except as to the amount of income to be currently applied to interest. He does not consent to any current reduction of that amount. But he again promises that the reduction to 4 per cent shall date back to the "date of bankruptcy", with this new addition, "if, in the reorganization, the claims of this Corporation have been fully paid" (R., p. 229).

At all events, the promise that Mr. Jones then made was plain and clear. It was binding in accordance with applicable statute law. And it was the one on which the Trustees would thenceforth rely, unless they were economic simpletons. Their petitions and sales and payments followed, to the extent of nearly $4,000,000.

As a result of these payments and the application of excess collateral income in accordance with the latest promise, the principal of the debt became less and less. The security became better and better; and it had become certain that the claims of RFC would be paid in full out of the collateral held by RFC, but not that such full payment would occur before the end of reorganization.

Thereupon, on January 29, 1945, the Trustees again wrote to the RFC reviewing the facts, giving specific figures, and "earnestly requesting" that the promised reduction to 4 per cent be made immediately retroactive instead of awaiting final payment, and that thenceforth the rate should be reduced to 3 per cent. This would have been a waiver of the condition of full payment in the course of reorganization as well as a reduction of the going rate of interest to 3 per cent. The words of this letter are as follows:

> "Having in mind current interest rates and the rates at which the government is able to borrow money, and also the substantial reductions in principal of R. F. C. and P. W. A. loans, as well as the fact that the loans are now so greatly over-secured, it is respectfully submitted that the interest rates of 5% and 4% per annum heretofore charged and applied by R. F. C. on the loans are excessive. Indeed the situation has changed radically for the better since December 21, 1938, when Mr. Jones wrote us that R. F. C. would accept a 4% rate from the date of bankruptcy if its claims were paid in the New Haven's reorganization.
>
> "Accordingly, we now earnestly request a retroactive reduction in interest to 4% since October 23, 1935, on R. F. C. loans and a reduction to 3% on both R. F. C. and P. W. A. loans from now on" (R., pp. 231, 232).

Although there had been a change in the administration of RFC, the new Chairman, Mr. Charles B. Henderson, did not then repudiate the promise made by Mr. Jones, expressly referred to in the letter just quoted. He refused to make the requested immediate reapplication at 4 per cent, without waiting for full payment "in the course of reorganization"; but he promised from that time on, to apply on the principal debt all income and payments received in excess of interest computed at 4

per cent instead of 5 as theretofore (R., pp. 232, 233). Of course, the Trustees assented to this small additional reduction; but there is not the slightest reason for supposing that it was either offered or accepted as a substitute for the larger reduction conditionally promised by Mr. Jones. It would have been a breach of trust for the Trustees to give up the benefit of Mr. Jones' promise on which they had already many times acted with Court permission.

Mr. Henderson's promise, such as it was, was immediately binding, just as was that of Mr. Jones, and for the same reasons. In continued reliance on both promises, the Trustees obtained a new Court Order, disposed of more securities, and made a large additional payment (R., pp. 217-221); and on July 11, 1946, they petitioned for Court Order No. 891 and permission to make final payment at the 4% rate, expressly reciting that such payment was necessary to fulfil the required condition (R., pp. 222-226). What might have been their action, even though neither Mr. Jones nor Mr. Henderson had made them any promise of reduction, no man can justly say. But it is higly unjust to use these letters as a basis for a charge that their subsequent assertion that they had relied on Mr. Jones' promise was an "afterthought". On August 2, 1946, when they first encountered a repudiation, they had some reason for afterthoughts.

Twice more, July 10, 1945, and June 18, 1946, the Trustees wrote to Mr. Henderson asking that the application of payments be made immediately retroactive (R., pp. 224, 225). Had any one of these three requests been granted by Mr. Henderson, it would have been unnecessary to petition the Court for permission to make the final payment out of estate assets. The condition required by Mr. Jones as a prerequisite to the promised retroactive reduction to 4 per cent, upon which the Trustees still counted, would have been waived. The requests being refused, the Trustees filed their petition for permission to make the final payment in time to earn the reduction.

It is submitted that the trust estate and its creditors should not be penalized by the nullification of Mr. Jones' binding promise, by reason of the lack of success of the Trustees in their repeated efforts to obtain a waiver of the condition required by Mr. Jones and an additional reduction that seemed to them fair and reasonable.

D. Absence of Reliance by the Trustees Is Not Indicated by Their Failure to Make Full Payment at an Earlier Date.

In their brief below, counsel for RFC asserted that by reason of their improved financial position the Trustees could have paid off the RFC loan, either out of cash assets or otherwise, during the years 1941 to 1945, and that their failure to do this shows that they were not relying on the promise of Mr. Jones. Such an inference is wholly unjustified. During those war years, the income available to the Trustees was indeed greatly improved. What action did they take? First, they purchased with Court permission large amounts of new equipment necessary to render the increased public service. Second, they paid off, by Court Order duly obtained for the benefit of the trust estate, certain other well secured debts bearing 6% interest. Third, as heretofore related, with the full consent and participation of RFC, they obtained Court Orders for the sale of parts of the collateral security and made payments on the RFC loan of nearly $2,000,000 over and above the large reductions that were being effected from the income from that collateral. Fourth, they voluntarily made available to RFC more than $1,800,000 by declaring dividends on The Connecticut Company's Class B stock owned and held by them. And finally, on July 11, 1946, more than a year before the close of reorganization, they petitioned the Court for permission to make the final payment to RFC in full in order to fulfil the condition of Mr. Jones' promise. At the hearing on this petition, August 2, 1946, they were prevented from mak-

ing this final payment by the objection of RFC itself. This action by the Trustees was well within the time limit set by Mr. Jesse Jones, nothing whatever having previously occurred to shorten that time. To show that the Trustees "relied" upon Mr. Jones' promise, it is not necessary for them to prove that all three of them had it consciously in mind during their working hours as their subordinates carried out their directions.

E. An Acknowledgment of Receipt of Mr. Jones' Letter by the Trustees Was Not Necessary.

The letter of Mr. Jones, December 21, 1938, required no written "notice of acceptance". He asked for no return promise by the Trustees, by which to bind themselves to make full payment of the debt. As he knew, they were permitted to make no such promise. Instead, he limited his own promise, making it expressly conditional on full payment of the debt, with interest at 4 per cent, in the course of reorganization. Whether he was bargaining for such payment or was merely inducing it as a result of his promise, he placed only one time limit on the fulfilment of the condition. From time to time, within that time limit, payments toward the fulfilment of that condition were made with his knowledge and participation. Never was it suggested that the promise had been ignored, or that it had been withdrawn, or that the payments were too late.

The record shows that the earlier promises of Mr. Jones had been politely acknowledged, "with thanks"; the fact that the record fails to show that his last promise was not so "acknowledged" is wholly immaterial. Mr. Jones knew both the attitude and the actions of the Trustees; he continued to participate and he bore no malice.

POINT VI.

Failure of RFC to keep its promise is harmful to the public interest and a plain miscarriage of justice to the debtor and its creditors.

The repeated promises of RFC were made by a high government officer with long business experience. There can be little doubt that Mr. Jones, personally familiar with the history of this transaction, would have adhered to his promise of December 21, 1938, had he remained in office. It was made to Trustees in Bankruptcy, public officers like himself, appointed by the Court to maintain public railway service, to effect a difficult reorganization, and to protect the interests of other creditors so far as possible. It was made by the head of a great government corporation, organized and maintained to assist in economic recovery, not as a profit-making institution.

If a private bank had not kept such a promise, even if it were not technically enforceable, it would have suffered general disapproval. Justice, equity and public policy require, as an English judge once said in his opinion, that "a government should be as honest as other people."

When the promise was made, interest rates were falling; and the Government was borrowing huge amounts at lower rates. The security held by RFC for full payment of its present loan was ample, the while the claims of its co-creditors were being scaled down and the investment of every shareholder was completely wiped out.

Amplified in extraordinary degree is the weight of these factors when the promise is one that is recognized generally, if not everywhere, as legally binding: so recognized by the law merchant for probably 2,000 years, so recognized by the Uniform Negotiable Instruments Law in every American jurisdiction, and so enacted by the applicable New York statute that extends to all contract

transactions alike the rule of the law merchant and the N. I. L.

Consider, *per contra*, the arguments offered for non-enforcement:

ARGUMENT 1: "The trustees never answered, nor did they ever promise to pay the notes, or tender payment." (Quoted from opinion of the Circuit Court of Appeals and asserted by RFC.)

Mr. Jones expected no answer and asked for no promise. His letter was one of a long series of letters, often being shown by the record to have been duly acknowledged. The very favorable one of December 13, 1935, was acknowledged "with thanks" by counsel for the Trustees. As Mr. Jones knew, the Trustees could not lawfully promise to pay the debt out of current assets. But he did request and require, as a condition of his promise, that full payment should be made in the course of reorganization. This required *action* by the Trustees, not promises or acknowledgments. And they took that action. Year by year, with full knowledge and participation by RFC, they obtained Court Orders, effected sales of securities, declared dividends and made payments on account to an amount approaching $4,000,000. Not one of these actions was a mere performance of a legal duty to RFC.

Not "tender payment" indeed! The Trustees *made* many payments, and RFC received them,—the promise of Mr. Jones, in the meantime, never having been withdrawn or repudiated. Not until August 2, 1946, after such payments had reduced the debt to a comparatively small sum and the Trustees had petitioned the Court to authorize full payment of the balance in strict accordance with the condition imposed by Mr. Jones, did RFC repudiate the promise or try to prevent the total fulfilment of that condition. Most of the debt was then already paid; and if "tender" of the balance were necessary to make RFC's promise irrevocable—which it was *not*—the petition then filed was the equivalent of such a tender.

Moreover, the repudiation by RFC did not succeed in preventing the complete performance of the condition. That condition was fully performed by April 30, 1947, by reason of income from collateral, received and applied by RFC itself. Before the final order of reorganization, RFC received from those sources, and applied on account, $370,537 in excess of full performance (following the order holding that its promise was not binding). And by the final Court Order the Trustees were compelled to pay the additional sum of $433,456, also in excess of full performance of the imposed condition. But for the repudiation on August 2, 1946, the Trustees would immediately on Court Order have made the required final payment, completing full performance, and making available for other creditors the amount of the interest thus saved and the income from collateral thus immediately redeemed.

ARGUMENT 2: "The promise of Mr. Jones was without consideration."

Even supposing that compliance with the condition (payment of claims in full) was not required by Mr. Jones as a bargained-for exchange for his promise [see definition in Restatement, Contracts, section 75], it is beyond belief that the continued action by the Trustees was not in reliance upon it, motivated by their duty and desire to conserve the interests of the Debtor and its other creditors. But it is quite unnecessary to decide whether their action was a "consideration", in the sense of either a "bargained-for exchange" or substantial "action in reliance". It is certainly a sufficient *cause for enforcement*, sufficient in the light of innumerable cases in the long history of the action of Assumpsit at common law, sufficient according to the principles and practice of courts of Equity, sufficient under all systems of the Civil Law,—and in excess of sufficient under the law merchant, the Negotiable Instruments Law, and the applicable New York statute.

ARGUMENT 3: We should not have to keep our promise as the New York statute requires, because that statute was not called to our attention in the District Court.

Even admitting, as counsel did, that New York law is the applicable law, we should not be compelled to obey the law (so runs this argument) because neither we nor they knew what the law was until we reached the Circuit Court of Appeals. It is not that RFC was not in truth legally bound and that counsel could have established as much (by evidence or argument or amendment) if the point had been raised in the District Court. It is not that RFC has changed its position to its injury, or that the conduct of the Trustees or of the Debtor was fraudulent or inequitable. It is only because counsel for both parties and the District Court were unaware of the statute.

To sustain such arguments would effectuate injustice to a high and serious degree—that plain miscarriage of justice frequently recognized by this Court and by the Courts of many other jurisdictions.

CONCLUSION.

It is respectfully submitted that the judgment below should be reversed and that a decree should be entered ordering repayment or remanding the case to the District Court for further proceedings according to law.

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APPENDIX.

***Hormel* v. *Helvering*, 312 U. S. 552 (1941).**

Excerpt from opinion by Mr. Justice Black:

"In the Circuit Court of Appeals, the Commissioner abandoned reliance on sec. 166 (26 U. S. C. A. Int. Rev. Code), urged that the Board was in error as to taxability under sec. 167, and argued that in any event the income was taxable to petitioner under sec. 22(a), 26 U. S. C. A. Int. Rev. Acts, 1940 ed., p. 669. The taxpayer argued that the applicability of sec. 22(a) was not open for consideration, inasmuch as that section had not been relied on before the Board. The Circuit Court of Appeals, though agreeing with the Board as to non-taxability under secs. 166 and 167, nevertheless ruled that sec. 22(a) could properly be considered, and held the income taxable to petitioner under that section. Because of a conflict among Circuit Courts of Appeals on the propriety of considering sec. 22(a) under these circumstances, we granted certiorari. . . . Two questions are presented for our decision: First, was the court below correct in holding that sec. 22(a) should be considered?

[*First.*] Petitioner in effect challenges the power of the Circuit Court of Appeals to pass upon any questions other than those which were directly and squarely presented in the proceedings before the Board of Tax Appeals. That court's authority to review decisions of the Board rests on statutes, which provide in part that the Circuit Courts of Appeals 'have power to affirm or, if the decision of the Board is not in accordance with law, to modify or to reverse the decision of the Board, with or without remanding the case for a rehearing, as justice may require.' . . . In general, it is the function of the Board to de-

termine the facts of a tax controversy on issues raised before it and to apply the law to those facts; and it is the function of the reviewing court to decide whether the Board has applied the correct rule of law.

Ordinarily an appellate court does not give consideration to issues not raised below. For our procedural scheme contemplates that parties shall come to issue in the trial forum vested with authority to determine questions of fact. This is essential in order that parties may have the opportunity to offer all the evidence they believe relevant to the issues which the trial tribunal is alone competent to decide; it is equally essential in order that litigants may not be surprised on appeal by final decision there of issues upon which they have had no opportunity to introduce evidence. And the basic reasons which support this general principle applicable to trial courts make it equally desirable that parties should have an opportunity to offer evidence on the general issues involved in the less formal proceedings before administrative agencies entrusted with the responsibility of fact finding. Recognition of this general principle has caused this Court to say on a number of occasions that the reviewing court should pass by, without decision, questions which were not urged before the Board of Tax Appeals. But those cases do not announce an inflexible practice, as indeed they could not without doing violence to the statutes which give to Circuit Courts of Appeals reviewing decisions of the Board of Tax Appeals the power to modify, reverse or remand decisions not in accordance with law 'as justice may require'. There may always be exceptional cases or particular circumstances which will prompt a reviewing or appellate court, where injustice might otherwise result, to consider questions of law which were neither pressed nor passed upon by the court or administrative agency below. . . .

Rules of practice and procedure are devised to promote the ends of justice, not to defeat them. A rigid and undeviating judicially declared practice under which courts of review would invariably and under all circumstances decline to consider all questions which had not previously been specifically urged would be out of harmony with this policy. Orderly rules of procedure do not require sacrifice of the rules of fundamental justice. And examination of the cases relied upon by petitioner discloses that this Court, in following in some cases the general principle sought to be invoked here by petitioner, has been careful to point out the circumstances justifying application of the practice in the particular case. Thus, for example, we held in *Helvering* v. *Wood,* 309 U. S. 344, 348, 349, 60 S. Ct. 551, 553, that the government could not present in this Court as a wholly new issue the applicability of sec. 22(a). But we there especially relied upon the fact that the government, when the case was before the Circuit Court of Appeals, had made an express waiver of any reliance upon 22(a). In *Helvering* v. *Tex-Penn Oil Co.,* 300 U. S. 481, 498, 57 S. Ct. 569, 577, this Court declined to consider a newly presented question, but pointed out that it had not been raised by the Commissioner either in his notice of tax deficiency, in his appearances before the Board of Tax Appeals or the Circuit Court of Appeals, or in his petition for certiorari to this Court. And in *General Utilities & Operating Co.* v. *Helvering,* 296 U. S. 200, 206-207, 56 S. Ct. 185, 187, though this Court said that the Circuit Court of Appeals should not have considered a contention not presented to or ruled upon by the Board of Tax Appeals, the statement was buttressed by adding that the Circuit Court of Appeals had 'made an inference of fact directly in conflict with the stipulation of the parties and the findings, for which we think the record affords no

support whatever. To remand the cause for further findings would be futile. The Board could not properly find anything which would assist the Commissioner's cause.' The plain implication of that decision was that the cause would have been remanded to the Board of Tax Appeals had the Court considered the newly raised point to be of sufficient merit. These decisions and others like them, while recognizing the desirability and existence of a general practice under which appellate courts confine themselves to the issues raised below, nevertheless do not lose sight of the fact that such appellate practice should not be applied where the obvious result would be a plain miscarriage of justice. Analogous in principle is the philosophy which underlies this Court's decisions with relation to appellate practices in other cases: those in which it has been held that a decision of the Board of Tax Appeals can be supported in the reviewing court on a new theory of law; those which have been remanded because the lower courts failed to give consideration to a phase of the case involving legal theories not presented; and those in which there have been judicial interpretations of existing law after decision below and pending appeal—interpretations which if applied might have materially altered the result. Whether articulated or not, the philosophy underlying the exceptions to the general practice is in accord with the statutory authority given to courts reviewing decisions of the Board of Tax Appeals—decisions not in accordance with law should be modified, reversed or reversed and remanded 'as justice may require'.

In accordance with this principle, we are of opinion that the court below should have given and properly did give consideration to sec. 22(a) in determining petitioner's tax liability. [Here the Court discussed the case of *Helvering* v. *Clifford*, 309 U. S. 331,

60 S. Ct. 554, in which sec. 22(a) was held applicable in a case similar to the instant one.]

As the record now stands we think the court below correctly concluded that the trust income was taxable to petitioner under the principles announced in the *Clifford* case. Therefore to apply here the general principle of appellate practice for which petitioner contends would result in permitting him wholly to escape payment of a tax which under the record before us he clearly owes. Thus viewed, this is exactly the type of case where application of the general practice would defeat rather than promote the ends of justice, and the court below was right in so holding."

The decision of the Circuit Court of Appeals, reversing the Board of Tax Appeals, was affirmed; but the case was remanded to the Board to give the petitioner an opportunity to introduce further evidence that might affect the applicability of Sec. 22(a).

Concerning the Amendment Made in 1936 to § 33(2) of the New York Personal Property Law.

This amendment (as well as an amendment in the same words of § 279 of the Real Property Law) was enacted on the recommendation of the New York State Law Revision Commission (1936 Leg. Doc. 65 C; 1936 Report, Recommendations and Studies, pp. 65-80), such Commission stating in part as follows (pp. 74, 75, 78, 79):

"Recent Legislation in New York

"In 1934 the Legislature by amendments to the Personal Property Law, section 33(2), and the Real Property Law, section 279, made binding, *without consideration*, agreements extending the time for the payment of any debt or obligation, whether secured or unse-

cured, and made binding, *without consideration*, agreements reducing for a fixed or determinate period of time the rate of interest on any debt or other obligation secured in whole or in part by real property, provided that a written note or memorandum of the agreement is made and signed by the parties thereto.

"This legislation left unchanged the rule requiring a consideration for executory agreements modifying or abrogating the terms of executory contracts, other than those specified. This fact at once raises a number of pertinent questions. If a written agreement between mortgagor and mortgagee to reduce the rate of interest is binding without consideration, why should a written agreement between landlord and tenant to reduce the rent require a consideration in order to be binding? If a written agreement between debtor and creditor extending the time for the payment of any debt or obligation be binding without consideration, why should a written agreement between the parties to a contract modifying other provisions of the contract require a consideration for its validity?

"Since the parties to any contract may by cancelling or rescinding the contract and executing a new one change any of their rights or obligations, with no consideration passing other than the exchange of the new promises, why should a modifying agreement be less binding? Should not the parties to a contract be able to do directly what they are permitted to do indirectly? Furthermore, since consideration is not a prerequisite to the validity of a gift of land, chattels or the obligation of a third person, why should consideration be necessary for the discharge of an obligor? These are examples of the questions which are raised by the recent action of the Legislature. . . .

"It is established law in New York that the parties to a contract, whether sealed or unsealed, can change its terms by rescinding the contract and entering into a new one. The exchange of promises under

the new contract meets the requirement of consideration. On the other hand, a modification agreement, without a rescission, is frequently unenforceable because of the rule that a promise to do what one is already bound to do is not sufficient consideration. In certain situations, as when the parties desire to extend the time of performance, or reduce the amount of money to be paid under a contract, it is difficult to provide a new consideration. It was obviously to meet this situation that the Legislature [in 1934] passed the amendments to section 33 of the Personal Property Law and section 279 of the Real Property Law * * *.

"If the policy underlying these sections be sound, and the Commission believes that it is, it is difficult to see why the modification of other provisions of a contract than those enumerated in the above statutes should not be binding without consideration, provided there are proper safeguards against false claims based upon alleged oral modifications. If a change in the terms of a contract which diminishes the rights of a party be valid without consideration, there appears no reason why a total or partial discharge of an obligation should require consideration.

"The Commission is not prepared to recommend the abolition of the requirement of consideration for making promises binding in the first instance. However, the Commission believes that once a binding contract has been made the parties thereto should be empowered to change the terms of that contract, or to discharge obligations thereunder, by mutual agreement without additional consideration, provided the agreement modifying or discharging the contract is in writing and signed by the party against whom it is sought to be enforced. With a view to accomplishing these ends, the Commission recommends that subdivision two of section 33 of the Personal Property Law

and section 279 of the Real Property Law be amended to read:

> An agreement hereafter made to change or modify, or to discharge in whole or in part, any contract, obligation, or lease, or any mortgage or other security interest in personal or real property, shall not be invalid because of the absence of consideration, provided that the agreement changing, modifying or discharging such contract, obligation, lease, mortgage or security interest, shall be in writing and signed by the party against whom it is sought to enforce the change, modification or discharge."

And see *Study Made in Relation to the Seal and Consideration*, 1936 Leg. Doc. 65 D, id. pp. 81-373.

Decisions of New York courts applying section 33(2) of the Personal Property Law include *In re Wanninger's Estate* (1942), 34 N. Y. Supp. 2d 326 (letter releasing loan obligations); *Thompson* v. *Willson* (1944), 183 Misc. 949, 51 N. Y. Supp. 2d 665, affirmed 269 App. Div. 829, 56 N. Y. Supp. 2d 415, appeal dismissed 269 App. Div. 937, 58 N. Y. Supp. 2d 352 (letter agreeing to forbear the prosecution of any foreclosure of a mortgage—under the 1934 act); see *Salinas* v. *Salinas* (1946), 187 Misc. 509, 62 N. Y. Supp. 2d 385, affirmed 67 N. Y. Supp. 2d 692 (letter in modification of a separation agreement and promising not to change the beneficiary in a life insurance policy); *Spector* v. *National Cellulose Corporation* (1943), 181 Misc. 465, 48 N. Y. Supp. 2d 234, affirmed 267 App. Div. 870, 47 N. Y. Supp. 2d 311 (agreement by creditor to subordinate his claims to other debts).

***Re Barbara Campbell*, 105 F. 2d 197, 124 A. L. R. 1243 (1939, C. C. A. 9th), cert. den. 308 U. S. 593, 60 S. Ct. 123.**

This is a case almost on all fours with the present one. Previous to her bankruptcy, the debtor had bought a ranch, giving her note for $33,500, with interest at 8

per cent. A dispute later arose; and the vendor's assignee signed a written document providing: "3. The lender agrees that if full payment thereof be made on or before Feb. 1, 1935, it will accept from the borrower [debtor] in full settlement and discharge of the note and obligations . . . the sum of $15,000 . . . with interest on said amounts from the date hereof until paid at the rate of 5 per cent . . . [plus other advancements, less receipts from produce sold] . . . provided, however, that if the borrower is not able to exercise the privilege hereby granted to pay and discharge said indebtedness on or before the date last mentioned, the lender shall not be deemed hereby to have waived its right to collect the whole indebtedness evidenced by said note . . . 4. Time is of the essence hereof."

This quoted provision was held to have created an option in the debtor to discharge the original debt as specified, the debtor making no promise to do so.

Before February 1, 1935, the creditor told the debtor orally that she would be given a reasonable time after that date in which to make the specified payment. But on February 14, 1935, without any notice of withdrawal, the creditor sued for foreclosure and for collection of the original note, with its 8 per cent interest.

The debtor thereupon filed her petition in bankruptcy; and the creditor claimed the amount of the original note with interest at 8 per cent. The debtor asserted that she had been "prevented" from making the specified payment by the creditor, tendered payment in court [this being in 1937, more than 2 years after the date that had been declared to be "of the essence"], and sought an order discharging her from further duty.

The District Court, reversing the findings of the referee, held that the creditor was not bound by its later promise and allowed its claim for the amount of the original note with interest at 8 per cent. This was reversed by the Circuit Court of Appeals.

The Court said: "We agree that the oral extension was lacking in consideration . . . But we think the weight of the evidence supports the finding of the referee that the debtor was at all times ready, willing and able to pay, and would have paid had it not been for the promise of appellee to extend the time, coupled with its failure to inform the debtor as to the net amount which had accrued under the agreement. The testimony of the witness Willcox, the debtor's attorney, together with other evidence of similar import, was sufficient to sustain the finding of the referee that the debtor was lulled into a sense of security by appellee's conduct and that she changed her position in reliance thereon. Under these circumstances appellee must be held to have waived the requirement of strict performance on February 1, 1935. It is estopped to assert that its promise of indulgence was without consideration. Williston on Contracts, Rev. Ed., Vol. 1, p. 494, ff; id. Vol. 3, p. 1990; Restatement, Contracts, § 90."

The position of the Trustees in the present case is much stronger than was that of Barbara Campbell. The promise made to her was oral; and she knew that it had been withdrawn more than two years before she offered payment in court. Her only change of position in reliance was that she had been "lulled into a sense of security" and had forborne to tender payment. Here, the Trustees had acted many times in reliance, to the great benefit of RFC; they had forborne to attempt any refinancing; they petitioned for Court Order No. 891, to make the final payment, before notice of any repudiation; and RFC in fact received the full payment as required. In addition, they held a promise in writing, in accordance with the applicable New York statute.

The Supreme Court saw no reason for granting certiorari in favor of the creditor of Barbara Campbell.